Neoliberalism and Trade Openness

Prices and Institutions in Chile post Dictatorship: 1990-2009

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Prices and Institutions in Chile post Dictatorship: 1990-2009

Doctoral Thesis

to obtain the degree of doctor
from Radboud University Nijmegen
on the authority of the Rector Magnificus prof. dr. J.H.J.M. van Krieken,
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to be defended in public on Friday, April 5, 2019
at 10.30 hours

by

Enrique Hernán Román González
born on October 17, 1954
in Santiago, Chile

Supervisor
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Para Ivette, sin cuyo amor y comprensión
esta investigación nunca hubiese concluido.

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To conclude this thesis, required a greater effort than I had originally expected. The bulk of it was written outside The Netherlands and therefore, the discussions about its content developed at a distance and was slower and more complex than those that were carried out by drinking a coffee or a beer in the Radboud University coffe shop, or simply discussing at my supervisor's office at the Thomas van Aquinostraat, in Nijmegen.

That's why I cannot but sincerely express gratitude to Professor dr. Ruerd Ruben, who never wavered in his permanent attention, patience and dedication to guide the development of this thesis, whose size and scope surpassed our common wishes at the time of beginning this investigation.

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I likewise be grateful to several friends and colleges, from different Latin American countries, with whom I had long discussions and exchange of ideas and experiences which allowed me to access information about the implementation of neoliberal policies in Chile and Latin America. It was particularly interesting to have access to the stories of those colleagues who, in various countries of the region, hardly worked in favour of the implementation of openly neoliberal policies, vis-à-vis those other friends who, in an even harder way, fought against them, sometimes within the governments of

different countries and in other times from the streets. Without accessing this broad spectrum of experiences, it would have been very difficult for me to acquire the perspective that guided my analysis of the Chilean experience.

In the Chilean case, I must to acknowledge the support of my old friend Jose Venegas, of the Department of National Accounts of the Chile´s Central Bank, for facilitate the access to data and methodology that lets to me disaggregate the Chile´s IOM of 2008 published on 2011. Obviously, any mistake contained in that work is my absolute responsibility.

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Before This Thesis

When in 1987 I left from Chile to the Netherlands to attend the MPhil in Development Studies at the ISS in The Hague, my country seemed irremediably on the way to civil war. The 14 years of military dictatorship that had imposed a neoliberal economic regime, had led Chile to endure not only a cruel repression that affected tens of thousands of people, but also some of the most severe economic crisis in its history.

Although in some international academic centres there was talk of the "Chilean economic miracle", in 1982 GDP had fallen by under 14%, and unemployment increased to levels close to 30%. However, when in 1985 the economy finally began to grow vigorously, paradoxically, opposition to the dictatorship seemed to abruptly increase.

At that time, huge weaponries and munitions, once abandoned by the US Army in Vietnam, were flowing into the country and began to be used on the streets. Alternatively, several Chilean leaders of the historical left, from Rome, Paris or Rotterdam, explored new options for non-violent democratization of the country and made their influence felt in the ranks of the democratic opposition to the dictatorship. However, they lack of a consistent analysis that would explain the economic boom that was observed in the country after 1985.

Between the beginning and end of 1986 the Chile´s GDP had grown by 5.6% and unemployment dropped to about 12%. However, the protests against the dictatorship, continued to increase with increasing violence.

However, despite this dark situation and against all expectations, moderate wing of the opposition take control of situation producing a dynamic that, during 1988, changed dramatically the Chilean political situation. On October 5, taking advantage of the scenario of "institutional normalization" that the dictatorship itself had programmed, four million electors finally voted for the end of dictatorship and for the call to free elections. On September 4, 1989, Chile again could elect a president by democratic means. At practically the same time, sixty days later, in an apparently unrelated act, the Berlin Wall collapsed and the Cold War was declared concluded.

After both events, the armed groups of the Chilean resistance dissolved slowly but inexorably, while hundreds of thousands of compatriots resumed a quick return to our country from states that, like The Netherlands, had generously offered them asylum.

I was in those years a student of just over 30 years who, in 1987, after actively participating in the civil fight against the military dictatorship, had left the country temporarily, together with a large cohort of young people who, in conditions similar to mine, had received academic scholarships from various European or US entities, in order to allow us to develop postgraduate studies in our different disciplines.

Two years later, by 1989, while studying at the ISS in The Hague, The Netherlands, I had already learned many things. First of all, I understand that the economy of my country could no longer be adequately analyzed from neoliberal fundamentalism, that saw success in everything that it did and enforced silence on everything that did not match their vision.

Second, also I have assumed a large distance from the orthodox visions that, refused to accept that "something new" was happening in the Chilean economy in terms of growth, employment and exports and that openness and market liberalization hardly be abandoned when the political situation changed.

After the end of the dictatorship in 1989, I abandoned the idea of completing a PhD in Holland, hurriedly finished my MPhil and three days after graduating I returned to Chile to join the new times that were outlined for my country.

Some things had changed, but many more remained as they were when I left Chile. Pinochet was still at the head of the army and the new government was walking on a minefield, in which day by day he was reminded that, if he abandoned "prudence", Chile could face a new coup.

In 1990, I was already part of that young technocracy described by Professor P. Silva (2010), a group which had been formed abroad and that, after their return to Chile, lead a good part of the new government. As a member of this group, I had adhered to many of the ideas that I strongly criticize in this thesis. The "ultra-gradualism" seemed essential to me, the success of the golden decade that lived the Chilean economy seemed to me inexhaustible and the prescriptions of the Washington Consensus, which had not yet been baptized with that name, seemed very truthful to me.

Between 1990 and 1995 I was part of the first and second government after the end of dictatorship, from there I try to promote a new industrial policy, the de-concentration of markets and the promotion of new productive sectors of higher added value and

exporting potential. But soon I realized that such efforts would be unsuccessful. The proposals of the Washington consensus had penetrated deeply into the government and it soon became clear to me which, from that point of view there was no greater possibility of changing the course of economic policy. Given that I had changed my old standpoints within the government, I faced only two options: To hush my criticism and continue ascending in the ranks of the Chilean government or to definitively self-marginalize from a political process that had shown me be absolutely ineffective to build the developed and non-discriminatory country which I aspired.

At the beginning of 1996 I had already decided to opt for the second way. Many hundreds of members of my generation followed the same path, renouncing their positions in the successive post-dictatorship governments. The Asian crisis of 1997 made even more clear that the new governments had absorbed the bulk of the neoliberal proposals. For that reason, several people who, like myself, had left the government, started to express publicly our dissent and emphasize a fact that in my country is not yet clear: While in Chile the centre-left defined as "neoliberal" only those policies inspired on the most extreme versions of the Austrian school, in the rest of Latin America, the proposals of the Chilean centre-left governments were also considered as neoliberal. Obviously, after express that ideas publically, I had no choice but developed my professional career outside of Chile.

From that year onwards, I become an international consultant and advise to different Latin American governments that, at the time, promoted productive development policies bolder than those implemented in Chile, and opened space for more innovative and progressive public policies than those that Chilean governments were willing to implement. However, the limits imposed by the public policies designed from a large distance of the social base slowly took me back to the grassroots and focus my work in projects of international cooperation and international NGOs.

After more than fifteen years of work in that kind of projects in poor neighbourhoods of Santiago, Bogotá, Medellin and Montevideo, with small Argentine farmers, with small Peruvian agricultural producers, with indigenous people from the Ecuadorian highlands and Amazon, forest, with SME entrepreneurs from different states of Mexico and with micro-entrepreneurs from practically all the countries of Central America, other dilemmas began to worry me.

Just as the public policies designed in the bureaus of the experts, generally ended up being captured by the great economic powers, on the other hand, the grassroots experiences that were not capable of influencing the design of the public policies, seemed condemned to the irrelevance. Together, while in a good part of the countries where worked, I received from some people hard criticisms of the "Chilean model" and its recipes and from other people I received compliments for policies that I did not share. Surprisingly, the compliments did not always come from the top elites, but on many occasions, they rather came from the base.

Towards the end of 2008, I was working in Bolivia evaluating a large training program for MSMEs, promoted by the first Government of Evo Morales. On two consecutive days, I had to face two extremely contradictory events. One night, I dined with the former finance minister of that country, an old friend with whom we had shared an office in the ISS in The Hague. He told me about the misadventures of his government in 2005, introducing policies that he defined as "sensible", but that had been denounced by Morales as being of neoliberal orientation. On the morning of the next day, I participated in an exhausting meeting invited by other friends, left-wing scholars, who were discussing the validity of an "indigenist" development strategy, grounded on the impulse to the Quechua-Aymara peasant culture, basing on principles of autarchic economy. When I left that meeting, in the street I faced an unexpected event. Outside the building, a small van was parked and on its side an Aymara peasant, with his colourful indigenous hat ("chullo"), a bag of coca leaves hanging at his belt, displaying an announcement in his hands, in which, wrote in a bad Spanish, was possible to read: "For expansion of markets I look for experienced drivers, try here."

The academic discussion from which I went that morning and in which, so many references had been made to the rules of the economic game which governed the "Tawantinsuyu", in which markets did not exist, now seemed bizarre to me. In the same way, the ideas of my Minister friend, who focused the defense of the market system on the hydrocarbons law that had caused his dismissal, seemed to me as more out of focus than before. Something was happening in Latin America under the noses of many, including mine, and our old paradigms could no longer account for the new phenomena. The emergence of new institutions, which pretend change the social and economic fabric clearly did not emerge as a by-product of the degree of anti-capitalism incorporated within the discourse of the governments: Neither seem to depend from orthodox macroeconomic proposals, in which the fiscal balance, the

prices system and the property rights, were the silver bullets of development process. I think that the idea which inspired this thesis was born at that split second.

Choosing a Dutch university in which there was a supervisor interested in some way to guide my exploration of these issues was a difficult task that took me almost a couple of years. Latin America was no longer fashionable and countries like Chile are already too rich to spend time studying processes that do not interest the academic world as much as they may be interested in, for example, African processes, a region to which today most of the resources of International cooperation are flowing.

Despite this, at the suggestion of the professor P. Silva, from the University of Leiden, I had the good fortune to meet the professor Dr. R. Ruben, of the Radboud University of Nijmegen, who agreed to lead my research, that, to tell the truth, did not fit the classic pattern of a young person who seeks a doctorate as a way to start an academic career. On the contrary I was an old field economist who, towards the end of his professional life, tries to account for the theoretical and political problems that he has faced throughout his career, without having obtained for them a consistent and convincing solution. I can only appreciate again, the kindness of my supervisor in accepting to guide my research in that context.

Addressing in a non-superficial way, all the issues related to the implementation of the neoliberal development strategy in Latin America was an almost impossible task for any PhD thesis, but even my decision to focus my research about neoliberalism, prices and institutions, only in the Chilean case, equally represented a challenging task. Analysing in a nuanced way the failures of the Chilean neoliberal model and without assuming a bias towards its positive aspects, was also difficult. A complex issue lay on the fact that our central focus was the falsification of the core of the neoliberal proposal, focusing in the veracity of their forecasts and in the real influence of changes in the prices system, vis vis the influences of institutional changes in the economy and society. Last, but not least, was the analisys of the neoliberal model in a country like Chile, where its post dictatorship governments had declared its anti-neoliberal perspective, but fostered processes that were associated to neoliberal proposals. Perhaps for that reason, the output of our research far exceeded the size of a standard thesis, and therefore I can only thank the tolerance of my supervisor, who, during the first two years of work, did everything possible to reduce the size of text in that I tried to resume my research

In spite of this, the thesis has concluded and I only hope that this research will enable understand, in a good way, the lights and shadows of the Chilean neoliberal experiment. Also hope that this dissertation be a contribution to the analysis of the difficulties associated with pretended importation of Chilean experience to other Latin American countries, such as Argentina, Ecuador and Brazil, whose governments have recently declared their aspiration to implement development models similar to those implemented on my country.

« Ce ne sont pas les prix qui déterminent tout,
mais tout ce qui détermine les prix »

Pierre Bourdieu
« Les structures sociales de l'économie »

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ACRONYMS

ACF:	Autocorrelation Function
ADR:	American Depositary Recipes
AFP:	Pension Fund Administrators.
AIR:	Active Interest Rate.
APL:	Average Productivity of Labour.
BCCH:	Central Bank of Chile.
CASEN:	National Household Socioeconomic Survey, developed by Ministry of Social Development, Chile.
CH$:	Chilean Pesos
CL:	Chile
CORFO:	Production Development Corporation of Chile.
CPI:	Consumer Price´s Index.
CTP:	Cash Transfer Programs.
D-W:	Durbin-Watson test.
DFL:	Decree with Force of Law.
DIPRES:	Budget Directorate, MOF.
DIRECON:	General Directorate for International Economic Relations of the Ministry of Foreign Affairs of Chile.
EC:	Export Coefficient
ECLAC:	United Nations Economic Commission for Latin America and the Caribbean (CEPAL).
EEC:	European Economic Community.
ENCLA:	National Labour Survey of Ministry of Labour Affairs, Chile.
ENIA:	Encuesta Nacional Industrial Anual.
FDI:	Foreign Direct Investment.
FECU:	Ficha Estandarizada Clasificada Uniforme.
FGT:	Foster-Greer-Thorbecke indexes.
FTA:	Free Trade Agreements.
FUT:	Taxable Profits Fund.
G20:	Group of Twenty.
GCPI:	General Consumer Price Index.
GDP:	Gross Domestic Product.
GDPPC:	Gross Domestic Product per capita.
GDPPPP:	Gross Domestic Product at Purchasing Power Parity.
GSR:	Government Structural Revenues.

GVP:	Gross Value of Production.
HBS:	Household Budgets Survey.
HDI:	Human Development Index.
HHI:	Hirschman-Herfindhal Index.
ICPI:	International Consumer Price Index.
ILO:	International Labour Organization.
IMF:	International Monetary Fund.
INE:	National Statistics Institute, Chile.
IOM:	Input-Output Matrix
IPAC:	International Price´s alignment Coefficient.
IRS:	Internal Revenue Service, (SII).
ISIC:	International Standard Industrial Classification
ISO:	International Standard Organization.
KI:	Kakwani Index
L:	Lerner Index
LN:	Natural Logarithm.
LSE:	Large Scale Enterprises.
MC:	Marginal Cost
MIT:	Massachusetts Institute of Technology.
MOF:	Ministry of Finance
MR:	Marginal Revenue
MSME:	Micro Small and Medium Enterprises.
MVP:	Marginal Productivity Value
NA:	National Accounts
NAFTA:	North America Free Trade Agreement
NCS:	National Customs Service, (DNA) Chile.
NDE:	Non-Developed Economies.
NEGT:	New Economic Growth Theory.
NENE:	New National Employment Survey.
NER:	Nominal Exchange Rate.
NGO:	Non-Governmental Organizations
NSI.	National Statistics Institute
NTCPI:	Non-Tradables Consumer Price Index
NTPAC:	Non-Tradables Prices Alignment Coefficient
NYT:	New York Times
OECD:	Organisation of Economic Cooperation and Development.
OLS:	Ordinary Least Squares

PAC:	Prices Alignment Coefficient.
PACF:	Partial Autocorrelation Function
R&D:	Research and Development.
RAW:	Real Average Wages.
RER:	Real Exchange Rate.
RUT (TIN):	Tax identification number
SAP:	Subsidy of the cost of the consumption of drinking water, sewerage and wastewater treatment
SBFI:	Superintendence of Banks and Financial Institutions
SEM:	Structural Economic Matrix
SH:	Structural Heterogeneity
SIF:	Single Family Subsidy.
SUF:	Supply and Utilization Framework.
TCPI:	Tradable Consumer Price Index.
TCR.	Real Exchange Rate.
TFP:	Total Factor Productivity.
TNC:	Trans-National Corporations.
TPAC:	Tradable Price Alignment Coefficient.
TWC:	The Washington Consensus.
UF (CLF):	"Unidad de Fomento", Chilean currency unit indexed according to inflation. At December 31 of 2009, amounted to US $40.
UNCTAD:	United Nations Conference on Trade and Development.
VA:	Value Added.
VMgP:	Value of Marginal Product

Chapter 1

Introduction

This research deals with the development of the Chilean economy throughout the first four post-dictatorship governments (1990 to 2009). The analysis will emphasise the particular relationships that these governments have established with the neoliberal development model, and with the associated institutions whose bases were built during the dictatorship period (1973-1989). Particular prominence will be placed on evaluating two specific areas. Firstly, we will focus our attention on the outcomes of the process of trade openness and the market liberalisation of the Chilean economy, analysing the correspondence between the actual results of the implementation of the Chilean model of development and the neoliberal forecasts. Additionally, we will analyse the process of the consolidation of the institutional environment and governance institutions, regulating the Chilean economy framed on the rules of the game inherited from the dictatorship period and consolidated during the selected period of analysis.

We predict that the analysis of the relationship between the performance of the Chilean economy and the functioning of its institutions, throughout the selected period, is a thematic area whose exploration can make a significant contribution to the analysis of contemporary worldwide experiences of economic development.

In order to describe the way in which we develop this analysis, we outline in this introduction our selection of key research issues and our research approach, followed by a short overview of the research hypothesis and the components of the analytical framework. Finally, we summarise the structure of this dissertation.

1.1. The Research Agenda and the Key Research Issues

To analyse an economy such as Chile's would be difficult without referring to the conceptual origins that have sustained their reform processes, which are explicitly associated with the neoliberal paradigm. Throughout this research, we will understand "neoliberalism" to be the intellectual project, born in reaction to the post-war welfarist and Keynesian consensus, whose fundamental premise is, "The superiority of individualized market-based competition, over other modes of organisation" (Mudge, 2008).

In this sense, the "neoliberal" appellation was commonly used in this research with an only descriptive purpose. It focuses instead on the need to establish a clear distinction between the neoliberal and the neoclassical approaches, a confusion that is quite common in many analyses. Neoliberal economic views are strongly founded upon neoclassical models, but even though the microeconomic and macroeconomic foundations of neoliberal approach are strictly neoclassical, both kinds of thinking cannot be analysed as though they were identical (Green, 2004).[1]

Neoclassical economics sometimes is called "mainstream economics", however, the label "mainstream" is a term full of twists and turns. As long as it is essentially a historically and sociologically defined category, mainstream entails the ideas that the "cream of the crop" in the profession finds suitable. However, that acceptability is mostly based on prestige and influence of the leading universities, journals and research centres which be in favour of certain approaches.

In that sense, outlining of *what mainstream economics is,* requires the assumption that this concept, in essence, verbalizes the volatile character of economic thought which,

1 Neoliberalism is a theory of political economic practices that assess that human well-being can be better achieved by maximizing economic freedoms within an institutional framework characterized by rights of private property, individual freedom, unfettered markets and free trade. This view assumes that the role of the state is to create and preserve an appropriate institutional framework for such practices, for example the issue of money, military functions, defence, police and judiciary required to ensure the rights of private property and support free functioning markets. In addition, it assumes that if they do not operate markets (in areas such as education, health, and environment), these should be created, if necessary, by means of state action. Nevertheless, neoliberals believe that the interventionism of the State in the markets (once created), should be limited to the basics, because the state could not possess enough information to anticipate the market signals, (prices) and because powerful interests inevitably will influence the State (particularly in democracies), with interventions for their own benefit (Von Mises 1944, Green, 2004).

in different periods of time, describes the leading beliefs that are promoted by the top schools and economic institutions, as intellectually sound and significant.

Obviously, all those institutions do not share a unique worldwide approach and even, within different academic and multilateral organizations, there are more than a unique approach and several research agendas exist in competition to one another. In view of that, the definition of mainstream is a highly controversial point and therefore, mainstream is not defined by incumbent scholars in the same way as defiant and heterodox scholars.

Heterodoxical criticism of assimilation of "neoclassical economics" to the concept of "mainstream economics", emphasize the actual crisis of the first approach, suggesting that it is debatable whether neoclassical economics is still mainstream. Several prominent non-orthodox economists, seem think that neoclassical economics fail to give sound answers to the economic challenges of present times, but political and academic resistance deployed by orthodox economists has been considerable. The strong support of neoclassical economics in the academic and political scenery, rest on the fact that it is not only a singular economic approach, it is essentially a "metatheory". It is a set of implicit rules and assumptions to be used for constructing different economic theories in which are based several economics approaches, being frequent that some defiant approaches end up weakened given their absorption of key aspects of neoclassical economic theory.

However, Chile present a singular situation to this matter. Neoclassical economics is not only overwhelming dominant inside the leading academic institutions, it is considered as the only serious theoretical approach to be supported by any well-trained economist.[2]

It is so difficult, from within the Chilean academic and political world, do not evaluate that approach as the guaranteed mainstream economics. Especially considering the fact that about 90% of Chilean academic and research centres, are controlled by scholars that support this view.

The fundamental shared conclusions of those who adhere to the neoclassical economists (a group that in Chile includes, as theoretical leaders, to several conspicuous neoliberal

2 Lüders R. (Former Chile´s Minister of Finances, PhD University of Chicago); Newspaper: "La Tercera", 25, october 2015.

academics), are not considered open to discussion; their assumptions are considered as a core elements of "positive economics" (Friedman, 1953) and, on that basis, they think that "positive economics is, or can be, an ´objective` science, in precisely the same sense as any of the physical sciences" (Friedman, op.cit.)

"Developing this discussion is more fruitful in the case of Chile than other Latin American countries. In these, the experiences of neoliberal reforms were brief, non-systematic, and associated with clearly negative results for each country. In Chile, on the other hand, neoliberal reforms have been carried out for more than forty years, have been of great depth and consistency and are usually seen as a success story for the neoliberal model. Moreover, the outcomes of this process are presented with satisfaction, not only by the neoliberal elites, but also by multilateral organizations, as well as by prominent economists' opponents of neoliberalism.

Based on this, in the course of this investigation, we have decided to test the empirical correspondence between the standpoints that constitute the theoretical framework of the Chilean Economic Model and their real outcomes in order to assess the real success of this model and therefore the adequacy of policy proposals, including the role of institutions associated to them.

In our opinion, with the aim of evaluate Chile's neoliberal economic model, was appropriate to use as a criterion the factual validation of its proposals, a benchmark that is otherwise accepted by its supporters as the only adequate.

Consequently, the focus of this thesis simply was to investigate if the predictions (promises) of the Chilean neoliberal model had been fulfilled or not. That is to say, analyse whether it is effective that the changes in the relative prices produced by the trade openness, accomplished to produce a new framework of allocation of resources or if, on the contrary, other factors of rather institutional origin, were ultimately those who predominated.

Then this thesis is confined to falsifying the forecasts associated with the neoliberal hypothesis, that means, evaluating the Chilean model from the validity of its predictions (in this regard, see 1.1. *"The research agenda and the key research issues"*).

It was not our intention to inquire about the internal logic of the neoliberal model, nor about the veracity of its ground-assumptions, nor about the causal relationships

that, from their perspective, explain the problems of development. Because that, we had not tried to submit to rigorous empirical evidence the veracity of the set of causal relationships proposed by neoliberalism, this would have exceeded the scope of a research of this nature, because each one of these topics merits in itself to elaborate an independent thesis. On the contrary, this dissertation is focused only on the exposition and analysis of empirical antecedents which could allow endorse or refuse the veracity of the forecasts of neoliberal theory in Chile.

This was done in that way because we felt that the political force and the intellectual attraction exercised by the neoliberal model does not lie in the quality of its hypotheses (mostly very well-structured), nor in the coherence of its vision of the economy and society (frequently exhibited). Its strength lies basically in the quantifiable results that it has exhibited in certain areas of the Chilean economy, and that, in other areas, it is expected to be able to obtain in the short run.

As Chile is the typical case generally cited as a success, it seemed appropriate face up to the empirical evidence, the outcomes of the opening process, especially those that are generally indicated as proof of the "Chilean model success". Therefore, if we only try to corroborate if the neoliberal projections, about the evolution of the Chilean economy associated to the implementation of its program of reforms (supposedly "market friendly"), did or did not materialize, would not be adequate on that bases, intend to extract general conclusions about ability or inability of the causal relationships between economic variables in which neoliberal proposal support their forecasts.

Neoliberalism postulate existence of well-defined relationships between different economic variables and elements (like the role of the market, private initiative, the State, the degree of openness of the economy, etc.) and the economic factors that should ensure the transition from a developing economy to a fully developed economy. For that reason, the neoliberal proposal consists in an unambiguous political program which intend to be implemented, from the State, pretending by that way to enhance the growth and development path of the Chilean economy:

Given that, we conclude that would be clear which, if the neoliberal projections about Chilean economy were not fulfilled, the positive association between the application of neoliberal policies and the obtaining of economic indicators superior to those that would exist in the absence of such policies, could be questioned.

Undoubtedly, this research path, from a theoretical point of view may look like somewhat modest; however, it is politically much more relevant, has a greater practical value and, certainly, may exert a greater impact on the ongoing political discourse underway in Latin America at this time, a continent in which the bulk of the discussions aimed at defining whether or not to implement the Chilean model of development are based on the alleged presence of outputs that wish to be imitated."

Throughout the thesis, chapter by chapter, we will show the fulfilment or disappointment of such projections. However, a definitive proof of the weakness or strength of the neoliberal hypothesis would not be possible through this methodological way (falsification of a hypothesis). We would need to use a more sophisticated set of instruments (basically econometric) to allow the establishment the veracity or otherwise of the causal relationships in which the neoliberal approach sustains its projections.

Even so, these conclusions would be valid only within the Chilean borders and for specific periods of time, requiring the study to be extended to a broad sample of representative countries and use long time series, in order to be able to draw conclusions of general validity or inadequacy of the neoliberal proposal. A study of that nature would far exceed the scope of this investigation, which in itself is already too broad. For that reason, this option did not seem realistic as a guiding perspective for our research.

Once we take the option of using a falsification methodology of the economic projections associated with the neoliberal hypothesis in order to express, in the form of a working hypothesis, the neoliberal-neoclassical standpoints generally applied to the appraisal of the Chilean case, we should hold that:

> *Chilean economic trade openness and market liberalisation made it possible for the Chilean economy, from 1973 onwards, to equip itself with an adequate macroeconomic environment and a pricing mechanism that ensured an efficient resource allocation mechanism. As a result, the Chilean economy produced a reallocation of its factors of production (capital and labour), from its most backward toward the more productive and globalised sectors. Because of this, labour of upgraded productivity witnessed greater remuneration, in turn improving domestic income distribution, the market competition and the competitiveness of its economy. This allowed the country to generate growth rates that led it to converge, both at the level of its GDP and*

productivity, with the more developed economies, especially those belonging to the OECD, to which Chile was incorporated in January 2010.[3]

The conceptual basis of this assessment is that: a combination of macroeconomic equilibrium with changes in relative prices induced by the process of trade openness, followed by a process of liberalising and resizing of the state role, would automatically result in a better allocation of resources.

Our intention was not to test the likelihood of the neoliberal hypothesis from the inside of its own story logic. As we said before, we do not intend to demonstrate that the economic variables to be analysed are functioning following the neoliberal proposed pathway. Our logic was the inverse.

We take for granted that, guided by its conceptual hypothesis, a neoliberal model of development was implemented in Chile forecasting to obtain certain results if a set of policies, guided by the neoliberal hypothesis, can be implemented. However, we firstly think that the quality of the neoliberal outcomes cannot be also take for granted, and secondly, we have doubts about the veracity of the hypothesis that holds that neoliberal model ever will obtain economic results superior to those of any other alternative model that could be implemented in substitution to it.

There is no doubt that is not possible to deny that the Chilean model, has been consistent and depth and, as we have tried to show throughout this investigation, this is due to the fact that the neoliberal project has been supported by a strongly institutional project. The Chilean model is not a group of isolated measures of neoliberal orientation, nor is it a mixture of policies whose final meaning is difficult to define. In Chile, a well-designed, tightly implemented and solidly argued model was implemented and is still being implemented. It does not present any gaps or severe discontinuities. On the contrary, its institutional course has been solid and consistent.

Nevertheless, the apology of the Chilean neoliberal model, presents some weak points in its argumentation, an issue which we have tried to show in this dissertation.

3 This working hypothesis is a synthesis of statements and projections of the main Chilean Neoliberal academics and politicians with regard to the impacts of the process of trade opening and liberalization of markets implemented in the country from 1973 onwards.

Its emphasis on market mechanisms and on the price system in particular, underlines the operational aspects of a market economy: "Right prices", "Free Markets", "market friendly economy" etc. look as sensible arguments, but these variables are presented and defended by local neoliberal, from outside of history and, particularly, from outside the institutions, an option which tends to situate the discussion on a merely theoretical level, assuming as granted that the analisys of real outcomes of the model is a minor issue, academically speaking.

In the arguments of the Chilean neoliberals, it seems that the only institutional elements that can positively affect the process of allocation of resources are those related to the introduction of new rules of the game that foster the free operation of the existing markets and the property rights associated to them. In sum, within this approach, institutions practically they do not matter beyond the presence of such factors.

If the claims previously reviewed by way of the working hypothesis are correct, no doubt it could be argued that the Chilean model of development has been very successful, focusing on prices and markets, moreover, if we believe in the accomplishment of forecast of Chilean neoliberals, would be sound to think that its conceptual bases could be extrapolated to other countries facing similar challenges. However, as we analyse later, the outcomes of the Chilean experience do not fit quite so well with the neoliberal forecasts and have been a little bit disappointed.

The combination of neoliberal macroeconomic policies and the associated institutional structure of the Chilean markets have indeed produced new relative prices in the economy. However, the performance of Chilean market is very contradictory to neoclassical and neoliberal forecasts. In fact, is not clear if the reallocation of a critical mass of resources from less productive sectors towards the more efficient and globalized ones, has been actually achieved.

The literature has described similar situations to the Chilean one in which often the result of trade openness is the lack of an export dynamic based on knowledge and innovation (Acs, and Audretsch, 1988), because of the non-reallocation of resources from low productivity to high productivity sectors. If this were the Chilean situation, it would imply that Chilean trade openness has been not successful in establishing a so-called "new and efficient relative pricing structure". Nevertheless, if the new relative prices cannot be labelled as "right prices" (if those kinds of prices exist at all), the situation would be the contrary. In this case, trade openness and market liberalisation

would have failed to create in the Chilean economy the desired "correct pricing"; because the new relative prices would not be acting as an efficient mechanism for the allocation of resources.

All this means that if we can find evidence that confirms the weak role played by the price system in the process of resource allocation, we would have found a clear point at which the neoliberal hypothesis fails in the core element that supports the credibility of their policy proposals.[4]
We understand that falsification of this hypothesis is a very ambitious and wide ranging intent, which attempt "nothing less than an overall assessment of the achievements – or otherwise stated– of Chile's long term embrace of market-friendly economic policies", even while understanding that it is not easy to develop a "well-grounded, focused and rigorous study of the Chilean experience".[5]

However, as we try to prove in the next pages, that is a hard but not impossible analysis, especially if our intent is well delineated and bounded to some specific aspects (subject to empirical tests) which allow us to derive general conclusions.

1.2. Neoliberal and Non-Neoliberal Approaches about Relationships among Markets and Institutions

From the late eighties, the view that institutions are the key to the development and economic progress of the nations has gained strength within development economic theory (North, 1990; Williamson, 1991; Rodrik, 1996; Hodgson 2004). This view holds that institutions influence the behaviour of economic actors by defining incentives that lead them to act in a certain manner; several authors have seen this behaviour as decisive in determining the success or failure of the nation's (North, 2003; Rodrik et. al., 2004; Acemoglu and Robinson, 2012).

4 In order to search for evidence to test hypotheses, the concepts generally used are "confirmation and falsification", coming from the philosophy of science (Popper, 1998). The search for evidence that is consistent with a hypothesis and that indicates that the hypothesis is true is called "confirmation", and the search for evidence that is inconsistent with a hypothesis and that indicates that a hypothesis is untrue is called "falsification"

5 Both points were asked to the author during discussions developed along this research work and were tried to be adequately resolved following the methodology lines described in this chapter.

Simultaneously, many authors increasingly argue that economic institutions are defined by the characteristics of the political institutions and thus, it is politics and power that create the capacities or incapacities of countries to implement economic development models which allow them to overcome poverty and inequality (Przeworski and Curvale, 2006; Acemoglu, D. y J. Robinson, 2008). Following this argument, politics is the place from which inclusive (or extractive) economic institutions can be built and consolidated.

Similarly, from within multilateral development financing agencies has emerged another "institutional" view, rather "economistic", that attempts to define, as they said, "on a technical basis" which are the most appropriate economic institutions for developing countries (Calvo G. and F. Mishkin, 2005). Nonetheless, the policies based on this viewpoint, of clear neoclassical roots, have gradually been incorporating elements of neoliberal thinking.

Neoliberalism assumed that actors are inherently self-interested and that their instrumental rationality has a "natural" character depending of human condition and in any way, must be considered as socially constructed or culturally and historically determined. They sustain that, if social and economic actors were allowed to freely behave, their performance would improve, and they would bring about optimal results.

In general, neoliberalism does not explain the institutional conditions that are necessary for the establishment of a competitive market itself. On the contrary, it tries to hide that situation by presenting the new institutions as spontaneous and evolutionary, naturalizing processes which are essentially political. However, as we will show in the next chapters of this dissertation, a free market system must not be necessarily considered as a superior evolutionary step. In fact, is not actually clear in which aspects it performs better than statists or corporate forms of capitalism, like those existing in Chile before 1973.

A wide set of research developed from the institutional field, is coincident with our perspective, showing that institutions captured by corporate interest might actually undermine economic performance (e.g. Dubbin, 1994, Abolafia, 1996 and Fligstein, 1996). Nevertheless, the free unfolding of market forces through trade and financial openness, deregulation and privatization, as has been implemented by neoliberalism, continue being, all over the world, a policy issue without a clear solution.

The policy proposals of neo-liberal character declare that trade openness promotes the efficient allocation of resources and would allow, through the development of competitive advantages, dissemination of knowledge and technological progress, and encouraging competition in domestic and international markets. In addition, recent theoretical models close to such inspiration, suggest a long-run growth effect, when the areas of specialization promoted by trade enjoy increasing returns to scale (Chang et al, 2009).

The non-neoliberal side assumes that the presence of market imperfections can lead to under-utilization of labour or capital, thus inducing concentration in extractive economic activities, and specialization away from technologically advanced sectors. (Grossman and Helpman (1991), Matsuyama (1992) and (Rodríguez and Rodrik, 1999).

The theoretical uncertainty on the effects of openness has also been argued from the field of available empirical evidence. Some papers point to strong growth effects of trade openness (Wacziarg, R & K. H Welch; 2008); and others point to ambiguous or small positive effects (Fetahi-Vehapi M et al; 2015; Bostrom, 2017). They stress which new coordination mechanisms induced by trade openness and by evolutionary economic processes contrast with the usual market mechanisms, based on relative prices, and the assumptions related to steady-state equilibrium of the traditional theory of growth.

Chile is a country significantly immersed in these discussions, which are deeply related to the process of economic reforms developed there from 1973 onwards. Because of those changes, the country has replaced its historical pattern of development, producing outcomes that have allowed multiple scholars (IMF, 2008; Fleischman, 2017) and multilateral organizations (World Bank; 2016) to define it as a "model country".
The policy proposals promoted by neoliberalism in Chile have brought about a buoyant debate on the pros and cons of opening of real and financial sectors. In addition, neoliberal policies have resulted in arduous disputes about convenience to reduce state regulations and associational activity. However, our research does not pretend to analyse all these issues. Our interest is narrower, focusing on the relation between institutions, markets, trade openness and economic performance.

We think that this is a debatable assessment that needs further appraisal because the Chilean economy expresses in a clear way a contemporary puzzle that is present not only in this country. Worldwide, Neoliberal and Neoclassical thinking are trusted more and more upon markets as a device that lets countries solve all issues related to

resource allocation. For this reason, our research aims to analyse the consequences of the neoliberal reform and liberalisation process of the Chilean economy that was implemented since the end of 1973. We think that these reforms should be evaluated, at first, based on the quality of their outcomes and the fulfilment of their predictions. Secondly, evaluation must be placed on the actual characteristics of their institutions vis a vis the weight of relative prices' influence on the resource allocation of the economy. And a third key issue to be appraised is dominance or subordination of institutions in relation to induced changes in relative prices resulting from as a result of trade liberalization.

From these three perspectives, we will evaluate the feasibility of a wider applicability of the Chilean experience, as a regional or worldwide model, like is proposed by neoliberalism. In our research, we develop some empirical testing and a theoretical reflection on the relation between economic institutions on the one hand and the economic performance of markets on the other. To this respect, we will use economic and historical findings and insights, with the intention of critically analysing the supposed success of the neoliberal model of development implemented in Chile. Firstly, we will develop a critical analysis of some of the leading assumptions that underlie the implementation of these neo-liberal policies. Secondly, we will analyse the most important outcomes of these policies, presenting the findings of our empirical research and extracting from them theoretical conclusions.

Notwithstanding the neoliberal approach considers important to introduce itself only as an economic project theoretically oriented to re-establish the "natural" market´s operation, strengthening full competition within them, in the real word it has been a large-scale project concerned with political, economic and social institutional changes- but not necessarily oriented in that direction. For that reason, we will intend to demonstrate that the Chilean neoliberal model of development is only disguised as an experience of market deregulation, however, even previous to the start of the implementation of the main economic transformations, the first priority propelled by Chilean neoliberalism was the introduction of a new institutional framework.

In fact, the neoliberal model of development must not be thought-out only as a "de-regulation" process of Chilean economy markets. The process was a little bit more complex, simultaneously to de-regulation, those markets were submitted to a process of "re-regulation" which redefine the existing big rules of the game and the wide range of arrangements that outlined the governance of those markets.

However, as we will demonstrate in this dissertation, contrary to what proponents of neoliberalism asses, the new market´s governance does not necessarily yield a more efficient economic behaviour of the actors. The total factor productivity stagnation is a clear sign of the impotence of trade openness to introduce a new and more efficient system of resource allocation.

Endorsing the Chilean Model based solely in the presence of high growth rates during a decade, or based on the consistence of policy proposals in relation to theoretical neoclassical assumptions, even though it is the preferred argument from multilateral institutions, is clearly inadequate.

The origin of neoliberal reforms, implemented by the military dictatorship that ruled Chile from 1973 to 1990, has been much studied in literature (Silva, 1987; Tironi, 1988; Valdez 1989; Angell, 1993; González y Fontaine, 1997; Arriagada, 1998; Vial, 2002; Agüero, 2003; Valdivia, 2003; Gárate. 2012). Nevertheless, the continuation of this process of reforms after the return of democracy has only begun to be critically analysed in recent years (Mayol, 2012a; Solimano, 2012; Garretón, 2013; Hunneus, 2014; Mayol, 2015, Guardia, 2015). Therefore, the period to be covered by this thesis is concentrated on the years between 1990 and 2009, which were the less studied in the currently available literature.[6]

1.3. Research Approach

Between 1870 and 1930, the neoclassical approach competed hard to consolidate a hegemonic role inside of the economic analysis. The result of this effort had not been less, as some authors have already said: already in the first decades of the 20th century Alfred Marshall, Leon Walras, Wilfredo Pareto and his disciples leaded not only of the economic theory developed in Cambridge (UK), but in the rest of the world (see Crabtree 1980: pp. 101-105). Its analysis is founded on a set of assumptions about the behaviour of individuals, which determine: prices, income, wealth and growth.

6 The next period 2010-2015, has too many singularities that would not contribute to our research. From 2010-2014 there was an important change in the administration of the State when the right wing returned to Government. During 2014-2015 "The New Majority", an updated and more radical version of the political coalition that ruled the country between 1990 and 2010, returned to Government. Analysing this new context would require several complex institutional variables to be introduced to the analysis, a task beyond the scope of this research and that would require a specific inquiry. For a more detailed analysis of 2010-2014 period, consult F. Ebert Stiftung (2012) and Mayol (2014).

These variables are understood from that perspective, as the originating economic institutions. This point of view also states that political institutions are defined by the installation of economic institutions based on individual decisions (Marshall, 1949; Hayek, 1967; von Mises, 1996; Menger, 1997).

The neoclassical school competed hard against the influence of historical institutionalism and against emerging Keynesian thought. However, after the publication in 1936 of "The General Theory" (Keynes, 1978), the neoclassical economics influence was replaced by Keynesian economics, from which, contrary to the neoclassical approach, based on methodological individualism, is assumed that in many areas, the economic structures determine the behaviour of individuals.[7]

The basic issues addressed by Keynes were the total volume of employment, the national income, the national production, the total supply, the aggregate demand, social consumption, social investments and social savings. Each of these variables begun to be analysed as part of the determining structure of the performance of the economy at the macro level. For Keynesianism, the evolution of these variables was not dependent on the behaviour of individual producers, or consumers, but rather from the will of the State.

Keynes did not share the view about an invisible hand guiding men to socially desirable outcomes. From his point of view, the action of the Government should be prioritised, because he saw as necessary that the rules of the game must be defended and implemented by the State, as a precautionary way of enforcing a good performance of the economy that the free market would not ensure. Thus, this new paradigm defined newfound ways in which the State could interact with the activities of economic agents, focusing on the rules and laws, which from the political arena, give the capitalist economy its particular institutional structure.

In the mid-1950s, based on the assumptions of the Keynesian paradigm, the Economic Commission for Latin America (ECLAC), as will be described in Chapter II, developed a particular version of that view, which is usually called: "Latin American Structuralism".

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7 In strict Keynes criticizes a broad amalgam of "classical economists" (e.g. Say, Smith) and "neoclassical" (e.g. Pigou, Marshall and Walras), nominating all of them as "classic", in effect he defines as classics (or followers of these) all those economists who cannot be defined as Keynesians. However, during the inter-war period the hegemony of his approach did not imply at all the disappearance of neoclassical thought, nor of the Austrian School, nor of the Old Institutional Economy.

This new vision integrated the Keynesian macroeconomic approach with a new analysis of the singular economic structures of the region. Keynes proposal emphasised the strong dependence of the peripheral economies upon the core economies; the decline in the terms of trade to the detriment of the producers of raw materials; the heterogeneity of the peripheral economies, at the level of sectors, scales and regions in which production was organised. To simplify, the ECLAC proposed a key role for the State in terms of macroeconomic policies and strategies of productive transformation of macro and micro impact.

From this last approach, an attempt to carry out an ambitious programme of transformation was promoted in Chile during the years 1970 - 1973, which attempted to modify the Chilean economic structure. This involved encouraging strong expansion of spending and aggregate demand, whose purpose was to alter the patterns of consumption, savings and investment whilst a social movement arose to enhance the transition to Socialism.

The Allende government that led this process of changes was not economically successful. In Chile, the expansive public expenditure policies in which were settled the CEPAL-Keynesian policies 1970-1973 (Ruiz, 2005) had made it increasingly difficult to finance a sustainable development process, while they had an ever-smaller impact on the problems that they were designed to solve: inflation, growth and underemployment. Therefore, its replacement by other economic models was urged and this tension deepened in Chile, framed by the possibilities that saw the commencement of the cold war in Latin America, leading to the emergence of the first worldwide neoliberal programme implemented in a national economy as a whole.
As we also discuss in detail in Chapter II, this process took place in Chile in the 1970s at the same time as the global half-century of the dominance of Keynesian thinking was ending. Therefore, the installation of the first neoliberal experiment in a real economy occurred in Chile amidst a dramatic political process, contemporaneous with the global crisis of the Keynesian model as well as a radical attempt to apply this to the Chilean economy. This model, as we will see in the next chapters, produced a large set of institutional changes in Chile, which have led us to analysing the role of Chilean neoliberal institutions as a critical determinant of the country's political and economic performance.

Neoliberalism was nurtured in Chile as a reaction to Keynesianism, structuralism and socialism,[8] proposing a heterogeneous set of institutions constituted by: rules of the game, formal institutions, normative institutionalised principles and cognitive principles based on neoclassical economics.

The Chilean process of neoliberal reforms was accompanied by far-reaching institutional changes in three areas: property rights, market institutions and the democratic decision-making processes. In each of these areas, from 1973 to present day, they have produced, radical changes in the entirety of pre-existing institutions that were replaced by others. This essentially political process ended in the authoritative enactment of a new Constitution in 1980.[9]

The processes of institutional change as described here are often conditioned by political and economic paradigms, which have to be institutionalised over time. In the Chilean case, the neoclassical paradigm, with its new macroeconomics based on assumptions of microeconomic behaviour of individual actors, was presented as a remedy to the ineffectiveness of Keynesian, structuralist and socialist policies. So that, on that conceptual basis, supported politically by a military dictatorship, the trade openness and liberalisation process takes place. The promise associated with

8 We do not hold that the policy of the Government of Allende was orthodoxly Keynesian, or much less that his downfall was related to the ineffectiveness of the Keynesian (or post Keynesian) approach incorporated into its programme. The fall of this Government is due to various additional causes: The sabotage actions financed by the U.S. Government and some American multinational companies; the lack of a common project of social change among the supporters of "Unidad Popular" government. Additionally, the radicalisation of social movements and, of course, the impacts associated with a policy of expansion of public spending that underestimated the monetary impacts of that expansion, played an extremely negative role. For a critical view of such processes from the perspective of the Unidad Popular's own supporters, see: Guardia, (1979: 45-92), from an opponents' perspective see: González y Fontaine, (1997).

9 On September 11, 1980 a plebiscite was held, convened only one month in advance, in order to approve or reject a Constitution drawn up by a "Commission of constitutional studies" and a "Council of State", whose members were appointed by the military junta. The opposition denounced the lack of guarantees for the legitimacy of the election act. Indeed, there were no electoral registers, there was not a census of voters, and there was no proportional access to the media by the opposition. The country lived in a permanent state of emergency, so that there was a restriction of civil liberties; the opposition did not have a district attorney to monitor the regulate development of the process and there was not an election qualifier tribunal where complaints of irregularities could be investigated. In summary, not only was the conception of the new draft Constitution irregular, but so was the plebiscite whereby it was supposedly approved, since it did not have the necessary minimum guarantees.

this policy was ambitious: growth, development, productivity, competitiveness and poverty reduction.

Unlike other neoclassical currents, such as the theory of endogenous growth,[10] the neoliberal program applied in Chile did not rest upon the idea of development understood as a process based on endogenous factors, but in changes in the system of relative prices. The installation of these prices was supported by non-inclusive political institutions, which went on to become the cornerstone of the neoliberal model implemented in Chile.

Based on this, a significant body of literature has been authored by various neoliberal economists attempting to show how results in the Chilean economy would confirm the adequacy of neoclassical theory and neoliberal proposals (Larraín y Vergara, 2000; Powell, 2000; Álvarez and Fuentes, 2003). However, in our opinion the scrutiny of that hypothesis must be done from a different perspective to the method proposed by followers of the "positivist" school (Carnap, 1956), used by the neoliberal authors already quoted. Such a method, proposing a "confirmation strategy" and trying to find as much evidence as possible to confirm the selected hypothesis, is clearly not appropriate. On the contrary, other perspectives (Popper, 1991) sustain that the compilation of a large number of confirming instances does not necessarily guarantee that this hypothesis is true. In fact, independent of the number of confirming facts, if just one major prediction of a theory is proved false, it demonstrates that the theory is incorrect or at least incomplete. For this reason, it was proposed that a falsification strategy, which would require searching for evidence that is inconsistent with a hypothesis (Popper, 1998), was better than a confirmation strategy.

As such, the falsification methodology ensures that some of these hypotheses may be abandoned in favour of better hypotheses, ensuring a progression towards truthful explanations that can increase our knowledge base. If the neoliberal-neoclassical hypothesis cannot be proven, we should proceed to explore other alternative hypotheses that might explain why this formulation is not defensible in the Chilean context. In light of this, an analysis of scientific views based on empirical falsification appears to be the optimal procedure for testing the truth of our working hypotheses, and an essential process for the growth of scientific knowledge (Lakatos, 1971). However,

10 The theory of endogenous growth will be discussed in the following chapters.

prior to proceeding to the falsification of this hypothesis, we need to describe in some detail certain contextual information that is essential to this exercise.

The presence of the existing contradictions between theoretical assumption and empirical facts is the basis of the analysis that we will develop in the subsequent chapters of this research. In them, we will make an effort to clarify to what extent a process of openness and liberalisation (like the Chilean one), is capable of promoting development and social progress, as neoliberal and neoclassical thought asserts. We will be then investigating if, against the grain of the neoclassical-neoliberal enthusiasm, reductions in poverty and income inequality remain elusive. Moreover, we will try to demonstrate that in Chile, the openness and liberalisation process over the last two decades has likely undermined efforts to increase productivity and growth, and to raise the living standards of the Chilean people in a sustainable way.

1.4. Main Issues to be analysed and Questions to be answered

If the presence of radical and consistent trade openness and market liberalisation were shown to be incapable of generating the outcomes predicted by neoclassical theory, it would be sensible to explore different approaches. Given the above, there are at least two general issues to be resolved in order to evaluate the applicability – in different contexts – of the process of neoliberal reforms analogous to the Chilean one. Both problems are related to the usefulness of neoclassical and neoliberal analysis and review the effect, on the development processes, that may be exerted by the policies inspired by this analysis.

1. The first issue to be analysed (*in the Chilean context),* is related to a crucial question: *Was it realistic to assume that changes in relative prices inducted by trade openness and market liberalisation were enough to promote improvements in competitiveness and productivity, and to enable convergence with more developed economies?*
2. The second issue to be analysed is related to a second question: *For a developing economy like Chile's, are keeping a pro-market orientation, defending property rights, achieving a certain macroeconomic balance and driving "macro reforms"*[11] *sufficient to*

11 The reforms promoted by The Washington Consensus (TWC) and the multilateral financial institutions.

achieve economic development, or are there other policies and institutional changes required, at the microeconomic and political levels, to attain this objective?

The answer to these two questions will largely define if it is possible to show the presence of inconsistencies between the neoliberal proposals and the empirically observable reality of the Chilean case. If we were able to refute the hypothesis formerly proposed at 1.1, it would be possible to change the focus of this research from the relative-prices area to another one: the setting up of appropriate institutions.

The change in the relative prices of the Chilean economy is a well-established fact; however, it´s not clear if this change produced a positive evolution in national competitiveness and productivity. The results exhibited by these variables since the end of the 1990s (Larraín et al., 2006a; Schmidt - Hebbel, 2009) seems to suggest that this outcome was not achieved.

The growth of the economy is also a well-established fact, to the point that no country in the OECD shows growth rates higher than those of Chile, at least over the period under study (OECD, 2011a, 2011b). Despite this, as we will analyse in detail in future chapters, it is not at all clear if these rates are enabling the convergence of Chile with the remaining countries of the OECD within a reasonable period of time.

Similarly, given Chile's relatively high GDP/ per capita within Latin America, its economy is considered prominent in the sub region. Additionally, some multilateral organizations (e.g. World Bank, 2013) consider Chile to exhibit a myriad of institutions of good quality, which have been aimed at ensuring the presence of a context that international bodies call "right" for the progress of all developing economies.[12]

However, in our view, the real impact of changes in relative prices remains unclear. We are uncertain as to whether Chile really possesses all the right and necessary institutions for development (that may be more than and different to those recommended by World Bank, OECD or IMF). In addition, we are unconvinced as to whether Chile really possesses, institutions whose quality be able to produce the type of economic growth championed by these organisations and which they declare to be oriented to the development of the country.

12 These include Control of Corruption, Government Effectiveness, Political Stability and Absence of Violence/Terrorism, Regulatory Quality, Rule of Law, Voice and Accountability.

We think that a more detailed and thorough analysis of the Chilean economy is necessary to answer the former two questions and a third one of crucial relevance:

3. *Are the changes in relative prices that define the rules of the game necessary to achieve economic development or, on the contrary, are the quality of institutions the variable that define proficiency of relative prices to influence economic development?*

Good institutions are those that stimulate agents' activities associated to a high level of social return by drawing together high private and social returns, ensuring a more efficient allocation of collective effort. From that point of view, it seems common sense to assume that such allocation will operate through the system of relative prices.

We believe these are the central questions to be answered. This will require describing essential elements of the country's economic structure, in such a way that enables us to understand the Chilean economy and its macro-tendencies. On this basis, the first stage of our analysis will be empirical, descriptive, and intended to evaluate the adequacy of the hypotheses that have been at play in the Chilean experience. Our focus will be put on showing the presence, or not, of the outcomes that neoclassical theory and neoliberal proposals have traditionally associated with the implementation of their policy recommendations. Hereafter, we will identify and discuss systematically a number of hypotheses that together make up the core of the neoliberal paradigm.

1.5. Components of the Analysis

We separate the core hypothesis into six specific components (that can be defined as separate assertions that form it), trying to analyse whether the evidence examined in this research substantiates the claims of Chilean trade openness and market liberalisation as a successful experience:

a. High economic growth
b. An increase in enterprise´s productivity and a high efficiency of markets.
c. A convergence of product and productivity
d. A widespread dissemination of technical progress and innovation in the productive fabric
e. A decrease in poverty and inequality
f. A new set of institutions of economic governance, enforcing the market´s competitiveness.

If all these assertions, or the best part of them, had been undertaken in the Chilean economy, we should conclude that the neoliberal proposals are satisfactory and have produced important benefits. In addition, we must assume that, as result, the Chilean economy and its process of trade openness and market liberalisation are signalling a viable path to development, that perhaps some other economies would be wise to follow. If on the contrary, the collected evidence shows us that these six positive results have not occurred, or have been insufficiently present, we should explore a different hypothesis. That would mean it would be necessary to explain why changes in relative prices do not operate with enough force to enable the achievement of each one of the aforementioned factors and the consolidation of efficient economic institutions.

To elucidate these issues in the course of this research, our analysis of the period under study (1990–2009) will focus on six thematic areas that seem essential to us:

1. The real relationships between trade openness, market liberalisation, the development of competitiveness, sectorial specialisation, export orientation and the dynamic of economic growth and employment generation of different sizes of companies in the Chilean economy.
2. The effects of trade liberalisation and the macroeconomic policies that complement it, on the convergence of the Chilean economy with more developed economies.
3. The effects exerted by trade liberalisation on resource allocation´s process and on the diffusion of technological progress in the Chilean productive fabric by means of the promotion of innovation and growth of total factor productivity.
4. The effects on productivity payoffs arising from trade openness and market liberalisation, especially in terms of relationships existing between the different sizes of firms (LSE and MSME), as well as effectiveness of antitrust policies that must be oriented to enforce fair rules of the game in the field of that relationships.
5. The effects of trade liberalisation on the growth process, income distribution and levels of poverty and inequality.
6. The setting up and upgrading of the institutional environment and institutional arrangements established during the 1980s and consolidated during the 1990s which define the real impact of trade openness and market liberalization over Chilean economy.

Here the bulk of the six selected areas will focus on the analysis of microeconomic problems while macroeconomic have been considered as secondary. There is a clear reason for this. The neoliberal programme originally implemented in Chile had a strong microeconomic component and its explicit purpose was the alteration of the system of relative prices to redesign the micro-fundamentals of economic life. It was assumed that the natural result of that would be an accelerated process of development, but after a strong initial effort in that direction, the impacts obtained in the area of growth and productivity proved is highly dependent on the macroeconomic context. Thus, subsequent interventions conducted within the neoliberal framework emphasised the macroeconomic themes over the microeconomic.

The first phase of implementation of the neoliberal model in Chile, focusing mainly at the macroeconomic area, let us define the "institutional environment", or in other words, "the major rules of the game" that determined the further development of the economy. This happens because governance institutions tend to operate at the level of individual transactions, which are then conditioned by the institutional environment in which they are immersed. Thus, we can say that the rules of the game that create such an environment exert a very important influence but only at a more aggregate level.

Ceteris paribus, the most significant rules of the game, the bulk of the issues involving the daily lives of economic agents, are defined by the adoption of specific forms of governance. Then, in the period under study, which we will analyse and discuss in terms of the evolution of the Chilean economy, the institutional environment only played a complementary role in relation to the definition of the rules of the game and the structuring of the institutions of governance.

In our research, the six already quoted areas of research are of microeconomic character. We have given limited weight to the exploration of the macroeconomic issues involved, because these are areas that have been thoroughly investigated elsewhere. (Corbo, 1985; Ramos, 1991; Sunkel 1991; Budnevich and Le Fort, 1997; Ffrench-Davis, 1982, 1999, 2003).

Each of these six areas will be analysed separately. In each one of them, we will emphasise the institutional determinants of existing articulations between the distinct Chilean economic performance and the characterization of it as an example of rules of the game which markets organised in a neoliberal way tend to embody.

In this sense, the identification of specific neoliberal institutions that have given a specific feature to the Chilean process of Neoliberal reforms will be the key that will let us define two crucial questions of high political relevance, which can be added to the above three questions which we have raised to resolve:

1. *Has the original neoliberal character of this model been conserved after the end of dictatorship, without modifying its nature?*
2. *Do the positive outcomes of this process depend upon the maintenance of the neoliberal model?*

The research findings of the six research areas will be reported in eight chapters in which, the five already quoted questions will be answered following the order and structure set out below.

1.6. Thesis Structure

The structure of this research is outlined in Chapter I. This chapter describes the research agenda and the theoretical approach to be used, the hypothesis to be falsified in the course of the research describe the methodology used to analyse the six thematic areas around which the research will be centred and the structure of the chapters that make up this thesis.

In Chapter II, we analyse the historical and economic characteristics of the neoliberal development model introduced in Chile in 1973. This chapter also shows how the process of implanting it and their associated policies have defined the strategic course of Chilean development during the last forty years. Lastly, we analyse existing relationship between trade openness and market liberalisation, comparing the different approaches developed by the leading schools that have influenced the Chilean experience.

In chapter III, we analyse the first of the already reviewed thematic areas, supplying a detailed vision of the Chilean economy, its characteristics and the impacts had on it by openness on GDP growth, and economic competitiveness. We also develop a particularised analysis of the institutional characteristics of the export sector and the labour markets operation.

In chapter IV, we analyse the second thematic area: the effects of trade openness and liberalisation on the convergence of product and productivity in the Chilean economy, trying to establish the degree to which this country is converging with more developed economies.

In chapter V, we analyse the third thematic area: we focus on the analysis of new system of relative prices installed by the trade openness, its relation with the processes of resource allocation, with the economic concentration progression and with technological progress diffusion mechanisms present within the Chilean productive fabric. The aim of this chapter is to analyse the effects of trade openness and liberalisation on the new prices which, supposedly, should act as signals orienting an efficient resource allocation process on the Chilean economy. However, given that there are severe doubts about whether this is effective, we will try to enquire if allocation´s processes are actually efficient or inefficient, and if they are determined by the price´s system or by the institutional structure of the Chilean economy.

In chapter VI, we analyse the fourth thematic area and report our process of exploration of relationships and arrangements existent between companies of different size and productivity strata of the Chilean economy. In that chapter, the characterization of outcomes of the institutional arrangements established between the different productive strata was achieved using the Input-Output Matrix 2008 (IOM 2008). That Matrix was used to characterize the consequences of institutional arrangements present in the different areas of production and consumption, among the three segments of firms (Smaller, middle-size and larger).

In chapter VII, we proceed to analyse the fifth thematic area, concerning issues related to the behaviour of the Chilean triangle: Growth, Poverty and Inequality, during the trade openness and liberalisation period under analysis (1990-2009). In this chapter, we try to determine the relationship between the persistence of inequality, regressive income distribution, the process of poverty reduction and the economic concentration existing in the country, showing whether these variables have supported the Chilean development strategy. In the course of this chapter, we also analyse the anatomy of income distribution in Chile: 1990-2009, the evolution of inequality in the distribution of monetary and non-monetary incomes, the impact of social spending on income distribution and the relationships between poverty and specific institutional arrangements prevailing in the labour market.

In chapter VIII, we focus on thematic area number six, describing and evaluating, from the political side, the roots of the concentration process at the level of the institutional environment and at the level of institutions of governance. Here we emphasise the way in which these roots were defined, at the level of the political constitution of the State and the rules of the game that have make stronger the increasing market and non-market power of Chilean business groups. This Chapter also deals with the constitutive elements of the rules of the game, both economic as well political, that defines the possibilities and limitations of trade openness in terms of exerting influence on the economic development process implemented by Chile. The process of economic concentration is analysed by observing how it links to the process of institutional capture of Chilean governments by the economic elites. Here, based on the previous analysis, we describe the restrictions that the Chilean institutions exert at the level of institutional environment and at the level of the arrangements that determine feasibility to obtain the development goals that the country seeks to achieve.

This research concludes, in Chapter IX, with a summary of the main findings and conclusions of our study, which we hope will enable, from an institutional perspective, a new evaluation of the failures and achievements of the Chilean development model and of neoliberal proposals.

Chapter 2

A Neoliberal Star Is Born: Genesis and Evolution of "The Chilean Model"

The objective of this chapter is to describe and analyse the historical and economic characteristics of the neoliberal development model implemented in Chile from 1973. Firstly, we explain why the relevance of this issue extends beyond the academic field, showing the presence in Chile of strong relations between academic thinking and the implementation of policies with a clear neoliberal label. We continue the analysis showing how these policies have defined the strategic course of social, economic and political Chilean development during the last forty years. In third place, we develop a short review of the theoretical debate concerning the existing relationship between trade openness and market liberalisation, and the discussions developed by the leading schools that have influenced the Chilean experience. These are the structuralist and neo-structuralist schools (based on the thinking of ECLAC); the neoclassical economic theory (both in its traditional and neoliberal versions); the New Theory of Endogenous Growth (with strong neoclassical roots, but differentiated in quite important aspects of neoliberal analysis) and the New Institutional Economics (in its various forms).

2.1. Chile in the Seventies: From Moderate Socialism to Radical Neoliberalism

Chile is a small country that has been outside the sphere of interest of the international attention for most of its history. This was not the case during the early 1970s, when the country inspired an unusual but significant amount of interest worldwide. This interest occurred as a result of the Chilean Government of the time's (Allende: 1970–1973) decision to implement a non-violent transition to socialism, guided by a mix of social democratic and communist perspectives, merged with the structuralist thinking of the United Nations Economic Commission for Latin America and the Caribbean (ECLAC). This proposal was called "The Chilean Way to Socialism" and consisted of a wide programme of social transformations (Allende, 1973; Touraine, 1974; Garcés, 2013). The defeat of such a programme and its replacement by a programme of neoliberal reforms, which expanded from Chile to the rest of the world, gave Chile a strong international profile, which was maintained for a long time. However, as we shall see in the next chapters, the reform processes that have been established in this country must be subject to a comprehensive analysis before being declared, as neoliberals do, part of a successful development strategy whose claim of adequacy and universality can be guaranteed.

That is the reason why we estimate that the examination of the Chilean reform process must be located within an accurate analysis of the historical context in which it occurred. In this chapter, we will address this in detail in order to define the scope of the conclusions to be drawn from this research.

During the early seventies, the Chilean experience of socialist reforms attracted significant worldwide attention, especially from Europe, sensitive at this point in time to the arguments introduced by Euro-Communism (Berlinguer, 1973) and the European Social Democratic left-wing, who were sympathetic towards the kind of development process implemented by Allende´s government through democratic means (Mitterrand, 1973). They saw in Chile a reform style that could be assimilated, and that was closely linked to their own programmes and historical processes (Kautzky, 2002: 42–44).

Global interest in the Chilean experience remained after the bloody coup d' état of 1973,[13] an event that ended the socialist experiment. In the following years, the military dictatorship that took control of the country started to drift away from the patterns that had typified similar regimes in Latin America, transforming Chile into a laboratory of emerging neoliberal policies. This phenomenon preceded and was implemented in a more radical way than in countries with similar economic reform processes, as the ones implemented in the UK and USA, countries who would adopted similar policies in the next decades.

In a few years (1973-1976), the Chilean experience embraced a set of radical, but not always consistent, economic policies. It is important to keep in mind that these policies were applied under special circumstances and in a small country ruled by a politically isolated dictatorship. This was before they became a formal model of social and economic development for the neoliberal camp (e.g. Piñera, 1978; Buchi, 1993; Mitchell and Morriss, 2012). Nevertheless, given the fact that at that time, Chile was practically the only neoliberal experience in the world, it did not take much time to turn this pivotal experiment into a highly-formalised development model.

This model, from the end of the 70's, was vehemently promoted beyond Chilean frontiers by some of the most conspicuous theorists of the then emerging neoliberal ideas, who advocated a global model of development following their proposals (Friedman, 1980; Hayek, 1988).[14] The apparent success of the Chilean economy has meant that this enthusiasm has not vanished with the passage of the years, and that "The Chilean

13 Forty years after the Chilean coup d ' état, the subject still seems to arouse some interest in European media, according to records from both the German Deutsche Welle, and the British BBC news (September, 2013). See: http://www.dw.de/chile-el-golpe-que-estremeci%C3%B3-a-la-izquierda-europea/a-17078266 and in BBC News: *Dalia Ventura*: *Why is the coup in Chile so emblematic*. September 11, 2013. http://www.bbc.co.uk/mundo/noticias/2013/09/130906_chile_11_septiembre_golpe_emblematico.shtml

14 A few years later, the Chilean "pilot-experience" had not only been replicated in several countries of the region, but also in the UK and USA. Additionally, many of its prescriptions were applied to the transition to capitalism of the Central and Eastern Europe countries. For example, the shock treatment that Jeffrey Sachs applied in Poland and Russia in the early 1990s, was a result of an extrapolation of the Chilean experience, previously applied to Bolivia. That shock was developed originally as a proposal for the Bolivian dictatorship of Hugo Banzer (1971-1978), but ended up being applied in that country some years later, during 1985-1989, along the democratic Government of Víctor Paz Estenssoro (Anderson, 2003).

Model" continues to be promoted by an important group of neoliberal thinkers, beyond the borders of the country.

2.2. What is the Chilean Model?

As Pepper notes (1966, 1982), "models" and "theories" are predicated on a "*root metaphor*" that constrains how scientists theorise and model a phenomenon and thus arrive at testable hypotheses. In this way, every social and economic model tends to be a simplified description of reality, designed to yield behavioural hypotheses amenable to testing. The most important features of a model tend to be conditioned by their association with the conceptual framework that defines the selection of events needed to explain their singular interpretations of reality. Obviously, the Chilean case is not an exception, the so called "Chilean Model" (Drake et al, 1999; Couso, 2008; Cea et al, 2008; Martner y Rivera, 2013) was initially envisioned by an orthodox neoliberal vision fully consistent with the former description. On this basis, the stylized group of assumptions and policies that were part of it, quickly assumed their intention to change in a radical way the Chilean economy and society (Cea, Diaz et. al, 2008). This model, which started as an essentially theoretical proposal, over time came to be regarded as an empirical example, whose strength essentially rests, according to its supporters, on its economic outcomes (Vergara, 1981; Labbé, y Vatter, 1988; Wisecarver1992). From there onwards, the main features of the Chilean Model were linked to three macroeconomic definitions that constitute the ideas-pillars on which it is supported:

1. The subsidiary economic role of the State in the economy.
2. The unilateral or negotiated openness of the economy to global markets, accompanied by a radical liberalisation of domestic markets.
3. The unrestricted search for macroeconomic balance through a systematic policy of controlled public expenditure with the priority of anti-inflationary goals, implemented by means of fiscal and monetary policies subordinate to these objectives.

However, each one of these elements does not solely constitute a neoliberal economic model. We can only properly define one as neoliberal when all these components are integrated into a unique macroeconomic package, which support microeconomic policies framed by specific rules of the game which conform an institutional environment characterized at least by:

1. The installation in all areas of unrestricted private property rights.[15]
2. The full determination of prices through market mechanisms, barring a handful of exceptions generally associated with the presence of natural monopolies.
3. The opening of the capital account of the balance of payments in such a way that the opening would be not only commercial but also financial.

In the Chilean case the presence of all six characteristics of a neoliberal model, the three pillars and the three-component of the micro-macro package, is not in doubt. But, additionally, the Chilean implementation of neoliberal polices included specific policies similar to those applied in the UK and the USA one decade later. The most important were:

- Substitution of welfare state policies by conditional subsidies focused on the poorest strata of the population,
- Massive privatisation of State-owned enterprises, especially utilities (gas, water and energy),
- Partial privatisation of education services (primary, secondary and university) and health and social welfare services, which were placed, largely, in the hands of private corporations.

In the Chilean case, other features were the adoption of "neutral" economic policies, the presence of a fixed rate of change (in the neoliberal-monetarist version), and a restrictive monetary policy (Meller, 1984a; De Castro, 1992).[16] The adaptation of

15 In the Chilean case, the property rights were incorporated as an essential part of the Pinochet´s Political Constitution (1980).

16 The early economic policy of the military dictatorship was contained in a document called: "The Brick". It is considered by many to be the basis of economic policy under the military dictatorship. The economist and future Minister of Finance Sergio de Castro (1976-1982) wrote the prologue, with contributions by various others economists also trained at the University of Chicago. This alternative economic program arose originally from the programmatic basis of the right-wing presidential candidacy of Jorge Alessandri (defeated by Allende in 1970), and was polished in the course of the "Unidad Popular" government as a shadow program. Weeks after the completion of the draft of "The Brick", the military coup took place (September 11, 1973). The new regime already had an economic program drawn up by specialists, who later formed part of the advisory team, as ministers, undersecretaries of state or consultants. This program arose as a post-socialist economic policy. Consulting measures included the release of domestic prices, decreasing the size of the public sector; elimination of operational deficit of the fiscal sector or public enterprises; a devalued exchange rate; the decline in external tariffs; the formation of a new capital market; the reversal of the agrarian reform of 1971 and the opening of the land market. A few years later, neoliberal trade openness, tax, monetary and fiscal reforms and the privatisation of

the Chilean economy to that scheme began at the end of 1973 and over the next five years, the Chilean Model jumped from being a mere theoretical proposal, to being the first national implementation of the emerging worldwide neoliberal programme.

As time passed, the Chilean military dictatorship redefined the form of the implementation of "The Model" but maintained its fundamental principles. In fact, the successive amendments and adaptations were adopted in a very pragmatic way, keeping the general validity of principles and institutions established by neoliberalism, allowing us to distinguish at least two distinct periods.

The first period ranges from September 1973 to March 1990. During these years, the Chilean economy began its liberalisation and subsequent openness, following the impulse of explicitly neoliberal policies driven by the military dictatorship (Hunneus, 2000).

In the second period from March 1990 to March 2010, the model was implemented in the context of politically weak transitional democratic regimes and the signing of successive free trade agreements that introduced some relevant reforms, but simultaneously deepened several aspects of the characteristics previously described (Hunneus, 2014).

Our research will be focused on this second period (1990-2009),[17] using the starting point of the openness and liberalisation process only as a reference. We chose to separate both periods based on an event of a political nature, the end of the Chilean military dictatorship in March 11, 1990.

This decision was based on the fact that, until very recently in Chile, the dominant opinion was that after the end of the dictatorship, the neoliberal character of the economic model changed almost simultaneously with the inauguration of the newly-elected post-dictatorship governments, modifying the neoliberal nature of the Chilean Model in the 1990s. We do not share this hypothesis.

The first period of this "model" was closely associated with a highly repressive, dictatorial political regime. This fact colours most of the economic policies associated

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welfare and social security systems were included.

17 The small period of time between January 1 and March 11 2010, during which the fourth centre-left Government, after being defeated electorally (at the end of 2009) by a right-wing coalition, was forced into the transfer of the Administration, will not be considered in our analysis

with this era.[18] It is for this reason that too many Chilean analysts, especially those associated with the new centre-left wing governments (e.g. Garretón 2013; Tironi 2016), sustain that the post-1990 period shows signs of a clear ending of neoliberal policy implementation, refusing to accept the hypothesis that assess that actually there are no essential differences between policies pre-and post 1990.

The acceptance of this last hypothesis would imply that, despite new democratic governments having at times operated beyond the narrow practical limits of the neoliberal view established during dictatorial rule, they have mainly continued operating within the ideological and economic frontiers imposed by a neoliberal vision of the State (Cypher, 2007).

Such a perspective has been defied by an important segment of left-wing Chilean leaders, because an acceptance would be equivalent to admitting that the neoliberal substance of the Chilean Model has not essentially changed since 1990 (but has only incorporated non-essential corrections). Accepting such continuity would imply that

18 From 2010, the advance in the velocity of change around this appreciation has been astonishing. When A. Mayol (2012) published his, book on "The Collapse of the Model", the socialist political scientist Alfredo Joignant argued in a debate at the Diego Portales University that the thesis of the "collapse" was "delirious". However, one year later Joignant published, as co-author (Atria et. al, 2013), a book in which were described the insufficient attenuations of the neoliberal regime fostered from the post-dictatorships governments, and attempting to propose replacing the exhausted neoliberal model by another founded in the "regime of public". In a similar way, Gonzalo Martner, former President of the Chilean Socialist Party, had shaped this official thesis arguing, "*Breaking with Neoliberalism did not occur in the area of commercial and financial opening to foreign investment or on the reversal of the massive privatisations (though a set of public enterprises of any significance has remained). This break took place, on a moderate scale, in the area of restoring previous levels of taxes and social spending (..), and in the change of rules for unionization, collective bargaining and a minimum wage, along with a regular social dialogue. The result of this option has been the doubling of the GDP per capita average growth rate since 1990, compared to that prevailing in the period of dictatorship of 1974-1989. The consequence of it was that Chile exhibits in 2007 an income per capita that is the highest in Latin America... and has increased its participation in the world economy since 1990". (Martner, 2009:85-89. Authors' translation and underlined).* In other words, this means that the rupture of the new Chilean governments with the neoliberal model would lie not in the presence of changes in the model of accumulation, but in greater operational efficiency induced by the new macroeconomic management and the distributive improvements introduced by the new administrations. However, in 2013, Martner´s vision changed and he sustained that in Chile the economic system was already captured by the economic powers. Additionally, he sustains that, without changes in this, there consequently would be the consolidation *of: "a model of market society imposed at the time by violence, based on negative individualism and the absence of socio-economics structures that would ensure civilized levels of equal rights and opportunities to all citizens.""* (Martner and Rivera, 2013:277).

the defeat of the dictatorship was less essential than holding his narrative, decreasing thus the political power and legitimacy of the elites who led this process.[19]

Our opinion is that even if it is true that, after 1990, the new centre-left wing governments produced some changes to the Chilean neoliberal model. It is difficult to demonstrate that these changes were linked to the end of that model, because there is no evidence of a genuine discontinuity of the institutional environment (the core formal and informal rules of the game) associated to the neoliberal model, as some authors argue it would have happened (De Gregorio y Landerretche, 1998; Muñoz, 2007). There is even less evidence that demonstrates the disappearance of the neoliberal institutional arrangements, the majority of which were established and consolidated after 1990.

As we will show in detail in section 4.2, the changes associated with the abandonment of the neoliberal-monetarist approach in 1982-84, introduced changes perhaps more radical than those amendments launched in 1990. That assessment will be clearer when we analyse the continuity of the neoliberal model implementation, when it produced a replacement of an explicitly monetarist-neoliberal agenda, with the approach outlined in The Washington Consensus (TWC).

In the Chilean context, assessments that deny the maintenance, after 1990, of the neoliberal nature of the model of development, tend to be supported by political appraisals that pay lip service to the extremely difficult circumstances under which the transition was agreed (Cavallo, 1998).

Successive democratic governments, post 1990, must move within dangerous "mine-fields" managed by economic and military powers beyond their control, while at the same time struggling to maintain electoral support. For that reason, their options were very complex. They had insufficient forces to fully challenge the neoliberal model and sometimes scant-motivation to implement radical changes but, on the other hand, any determination to resign (in an open way) from their original programme of changes was unacceptable for many of the foot soldiers of the new administrations. Then it

19 This dilemma is not specifically Chilean. Throughout Latin America, the bad image of "neoliberalism" has been increasing. However, the leftist governments of the region, both the moderates and the radicals, are facing many problems in defining what the non-neoliberal policies that must be implemented are. (Buendía et al.; 2013).

became extremely difficult for these governments to maintain balance between those two atmospheres.

From this derives the on-going ambiguity as to the economic programmes of the Chilean Governments that succeeded the military dictatorship. As a result of this, our research assumes the point of view that appraisals about the "rupture" of the post-dictatorship Chilean governments with the neoliberal model, should only be taken into account as a hypothesis that needs to be proved and should not be accepted without question.

The neoliberal package described above is a consistent group of political, macroeconomic and microeconomic interventions. Behind these interventions, it was in the public interest to merely mediate between groups of private agents. The role of the State in this process of mediation was visualised as being minimal.

According to this, the key question that defines whether, after 1990, the Chilean model has continued being a neoliberal one, cannot be linked to the attempts to maintain, or raise, the ceiling of any minimum thresholds of social negotiation. That issue is more complex than that and can only be solved by analysing the continuity or discontinuity of the rules of the political and economic game. This means that the issue is an institutional one.

From the post dictatorship governments, the core area of changes of the neoliberal model were understood as linked to a general rise in tax levels, improvements in the level of guaranteed health, or to the expansion of a level of compulsory and free education. Nevertheless, this orientation was something very different to promoting processes oriented to change, in the short or long term, the mechanisms of the definition of the minimum threshold.

The first option would only introduce non-essential corrections to the model; the second would lay the foundations for a radical change of the rules of the game. In light of this, one of the major concerns of this thesis is to establish what the dominant force that has prevailed during both reform periods has been: change or continuity.

In other words, this is an enquiry into whether the neoliberal fundamentals of the Chilean model have remained unchanged or not, after the return of democracy; a crucial problem that has become the centre of the political and academic discussion

of the on-going Chilean debate (Drake and Jaksic, 1999; Ottone y Vergara 2006; Mayol, 2012b; Atria et al., 2013).[20]

2.3. The "Anomalies" of the Neoliberal Model from 1990 to 2009

The arguments that, both in Chile as abroad, claim that, after 1990, there was a kind of reversal of the neoliberal identity of the Chilean model, are based on the presence of some economic phenomena that, at first glance, seem not to correspond to the classic attributes of an economy that follows neoliberal orientations. Several of them will be analyzed in the following chapters, however we will refer here to two main topics that, for this purpose, are frequently used in the discussions about Chile.

2.3.1. Why the largest copper company in the world be a State-owned Chilean company?

Chilean copper was completely nationalized in 1971 by President Allende. During the dictatorship, period this public property was not modified, but in 1975 a specific law was promulgated that destined 10% of sales of copper to a fund destined to finance military equipment and current expenditure of the armed forces.[21] Using these resources the Chilean armed forces have gained recognition as one of the most powerful in the South American continent. Given this, there was a permanent military opposition to any neoliberal attempt to re-privatize Codelco in such a way that could result in the armed forces losing control of these substantial amount of resources.

Nevertheless, the privatization of the Large Copper Mining had its origin during the dictatorial period, when in 1981, after the promulgation of the neoliberal constitution of 1980, the so-called "Organic Constitutional Law on Mining Concessions" was promulgated, launching a new concession category, called: "full concession". This law

20 It is not an easy job to analyse the crucial point, which has led to the popularity of the Chilean Model: its achievements in the area of economic growth. Obviously, it is not the same to conclude that these realisations are due to the orthodox application, after 1990, of the neoliberal premises. which believe that the eventual Chilean "success" obey to the abandonment, by the post-dictatorship governments, of the essential elements of the neoliberal theoretical grounds.

21 This situation was enacted in April and had the character of "secret" until mid-2016. It was not published until 2016 and during the first 16 years of democratic governments not even parliamentarians could access its contents.

allows those who discover mineral deposits to obtain the concession of these practically without cost, and can exploit and economically benefit from them. If eventually, the Chilean State would like to recover the deposit later, it should pay to the company that has the concession, the equivalent of the present value of the invested capital and the present value of the deposit not yet exploited. This is despite the fact that the 1980 Constitution states that copper will always remain the property of the State, or regardless of the fact that 40% of large cooper mining it is administered by a State company.[22]

In simple words, the dynamics are as follows: The State of Chile has large copper deposits, it lends them free to large mining companies to exploit them and if the State wants them back, it must pay multinationals the value of everything the copper that had been granted to him (since they did not even pay for the concession right). This means that, in practice, copper deposits are expropriated.

However, these guarantees, the large mining multinationals did not invest in Chile while the dictatorship was in functions, given the uncertainty that its long-term investors had in relation to the uncertain scenarios that, at that time, presented the transition to democracy. Foreign investment began to arrive only after 1990. However, by the end of the dictatorship such large number of mining concessions had been delivered to the private sector (national and international) that, in 2009, once these investments were deployed, only 40% of the national copper production remain at the hands of public sector, while 60% was private.

However, increasing that proportion, selling Codelco to the private sector, is not an easy task. Codelco finances with its surplus the strong military expenditure of the country and also a significant part of the social expenditure of the State. It is not clear at all how both items could be financed in the event that Codelco does not deliver such amounts to the national treasury. Codelco between 2002 and 2011 produced 35% of the total copper and contributed to the Treasury 63.4% of the income derived from

22 Prior to the enactment of this law, 100% of the Chilean copper mining reserves belonged to Codelco. The immediate effect of the law was to privatize 60% of Codelco's assets. Moreover, if the leased but not yet exploited deposits are accounted for, it is likely that this proportion would rise to 80%. The fact that these mining rights were not immediately exercised has a simple explanation. To request mining rights did not have a higher cost for the large cupriferous multinationals, but the realization of major investments could be associated with some great financial risks in the event that the neoliberal project failed, and the dictatorship was replaced by a new government whose program included the renationalization of Chilean copper. By the end of the 1990s it was clear that this would not happen and therefore the cupriferous investments began to flow in an overwhelming way for the economy.

Large-Scale Mining. On the other hand, the Large Private Mining produced 65% of the total copper and contributed to the State 36.6% of the income of this sector. In simple words, Codelco producing approximately one third of the total copper production contributes to the State almost two thirds of the total income that it receives from the large mining industry.
Privatizing Codelco is not an easy task, without the Chilean State discovering how to replace revenues equivalent to 10% of Codelco's sales (destined to military spending), which constitute 80% of the company's transfers to the State. The remaining 20% of their transfers should also be substituted to finance the growing social spending. Given this, the privatization of Codelco without replacing those sources of income, would risk an economic crisis of the Chilean State that would collapse it, generating a social crisis of magnitudes impossible to evaluate.

A second limit to the privatization of 100% of the large copper mining industry, through the privatization of the 40% that Codelco still has, is a task that requires capital magnitudes of such magnitude, that it would be difficult for a Chilean economic group to deal with this problem. The only eventual buyers would be large multinational companies and obviously, the local business groups, which control the economic life of Chile, have no greater interest in promoting a process of that nature, of which otherwise they would not be a part.[23]

Therefore, a last element of the neoliberal strategy in relation to Codelco has been to privatize it internally through out-sourcing practices.[24]

In "El Teniente", the main underground copper mine in the world (owned by Codelco), in December 2005 the subcontracted workers were 9,495, distributed among 333

23 This situation shows that, the great political ability of the Chilean neoliberal project, to disguise its model, when it faces high levels of political opposition, does not mean that such tactical agility should be confused with a renunciation of its program.

24 According to the CEO of CODELCO, the company has about 19,000 of its own workers and 38,000 of its subcontracted workers (50% of the total). If all the labour costs of the company are added, including the costs of negotiations, the average Codelco worker costs roughly US $ 5 thousand per month; and the outsourced worker, about US $ 2,500 (50%). However, the productivity of a worker of his own is around 90 tons of fine metal per person per year and in the case of an outsourcer, in about 50 it is worth saying that internal productivity is equivalent to 180% of that of subcontracts). From here it can be deduced that there are no reasons for cost savings that explain subcontracting and that this mechanism generates large levies on the surplus that Codelco should generate.

external companies that currently perform some type of function or provide services to the public company.

Of these subcontracted workers, 49.6% comply with activities related to support services, related to food, industrial cleaning, offices and transportation, among others. 27.4% are involved in tasks related to mining preparation, that is, development (horizontal and vertical excavation) and civil works (fortifications and minor works). Another 12.6% works in maintenance and repair of buildings; while the remaining 10.4% performs, work aimed at providing other minor services. However, Codelco's own workforce in that mining division ascend only to 4,933 own employees.[25]

The operation of this mine of the state company is repeated in the other mines, in which only 52% of the workers belong to it and the remaining 48% to private companies, gives a pretty close idea of the level of value-added transfer from Codelco to the private sector.

Then, the subsistence of this large public enterprise, cannot be alluded as incongruous with the neoliberal model; this should be shown as a factual limit to the implementation of a neoliberal model in 100% of the areas of the economy.[26] This situation, however, has not discouraged Chilean neoliberals from privatising a large part of Codelco and continuing to press for even higher levels of privatization.

2.3.2. Why was implemented in Chile controls on capital flows in the mid-1990s?

It is also habitually argued that the control of capital flows by a developing economy implies a substantial rupture with the neoliberal model, therefore, the conclusion of that assessment is assuming that, introduction in Chile of some forms of state regulation of the short-term external capital, would be an unequivocal signal of rupture of the new administration of the Chilean State with the neoliberal model.

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25 "División El Teniente - Codelco Chile", (2006); "*El Teniente y sus Contratis*tas*".* Document in Microsoft Power Point. Format. Rancagua, enero, 2006.

26 To argue otherwise would be tantamount to maintaining that the Government of Ms. Thatcher in the UK cannot be called neoliberal, since it did not proceed with a full and final privatization of the NHS.

Analysing this issue in Chile in the 90s requires differentiating two stages. The first of these covers from the beginning of the 1990s to mid-1997 and the second the subsequent period.

During the first year of the decade, major changes in the macroeconomic policies inherited from the dictatorial period were not a priority by the new authorities. On the contrary, in the following years, the outflow of capital was significantly liberalized, and the exporters were able to freely dispose of their total returns, without any obligation to enter the country. In addition, liberalization measures were taken in several areas: for example, the minimum term for the repatriation of capital paid by non-residents was reduced from three years to one year and the issuance of bonds and shares abroad (ADR) was authorized, whose requirements they were gradually relaxing over time. On the other hand, the exit of investments by virtue of the conversion of external debt (mechanism linked to the crisis of the first half of the eighties) was liberalized and the prepayment of debts abroad was also liberalized, as well as the minimum percentage of external credit that should accompany direct external investment (Ffrench-Davis, 2003). In short, a set of measures that did nothing but deepen those that the neoliberal model had implemented during the dictatorship.

Driven by this context, in that period Chile recorded an important inflow of external resources (on average 7.3% of GDP), which clearly exceeded the amounts of external financing estimated as reasonable and sustainable. In the same way, real private spending, which represented more than 75% of domestic aggregate demand, showed high increases in that period, which averaged 10% per year, exceeding the increase in public spending and also the effective product and potential (BCCH, 1990- 2010).

This high growth in spending allowed a strong appreciation of the Chilean peso, so that the authority, began to experience severe difficulties to maintain monetary control of the economy.

The Central Bank responded through periodic application of adjustment policies, by way of increases in interest rates, in order to prevent higher rates from encouraging even greater inflows of external capital, diluting the effect of such adjustments and generating greater pressures to the exchange appreciation.

Beginning in June 1991, the Central Bank of Chile introduced a system of high requirements for "no remunerated bank reserves" (NRR) for foreign investors, which

constituted an adjustment to the entry of selective external capital. This consisted of a mandatory deposit, in dollars (unpaid) and proportional to the amount of certain capital inflows, forcing foreign investors to maintain such deposits for a year. This produced an increase in external financing, discouraging the entry of short-term capital, as the monetary authority intended.

For the authority, the composition of capital flows mattered a lot in terms of the volatility and persistence of short-term flows, unlike long and medium-term flows, which are less volatile and much more persistent. However, the measures adopted following the old neoliberal monetarist recipes had favoured a composition of external financing strongly concentrated in short-term flows.

This was not innocuous. In the beginning of the 1990s, Chile's domestic private spending was strongly influenced by the size of capital flows, which respond significantly to the spread and reserve requirements. Given all this, regardless of the opinion of some neoliberal hard-liners, heirs to the predominant monetarist approaches in the authorities of the dictatorial period, it seemed common sense to assume that an eventual removal of the reserve that Chile had been gradually implementing since 1991 would have aggravated the over-expansion of spending in its economy: Then the contribution and macroeconomic effectiveness of the reserve should be measured in terms of its contribution to reducing aggregate spending.

What happened was that in a completely open economy such as Chile's, which received a strong influx of external capital, monetary policy was no longer able to avoid the expansive impact of such investment on the price of assets, since it was increasingly losing its autonomy and effectiveness in terms of controlling domestic demand.

To support at that time the old monetarist recipes which contended that a contractive administration of the interest rate, plus a fixed exchange rate that forced adjustments in the real sector of the economy, was already out of place: That recipe had failed in Chile during the crisis of the eighties and the bulk of Chilean neoliberal academics had already abandoned such approaches.

By the mid-1990s it was already clear that monetary policy was limited in terms of its effect on domestic spending, given the impacts that were produced by the over-inflow of capital. This weakening was not due to the absence of a fixed exchange rate (as

neoliberal hardliners wanted), but was due to the fact that the exchange rate did not have full freedom to fluctuate in response to changes in the interest rate.[27]

If the Chilean peso had not been able to appreciate freely to compensate for the effects on the spread of rates exerted by the increases in the domestic interest rate; an inflow of additional capital would not have weakened the effect of the contractionary monetary policy on domestic spending and therefore would have complicated the effort to stabilize the exchange rate. In this sense, the reserve was designed as a compensation tool for the effects that the spread had on capital inflows, thus allowing a contractionary monetary policy with lower exchange rate effects.

The second period, 1997-2000, was characterized by an increasingly adverse international context, triggered by the financial crisis in Asian countries, as a result of which the global flow of capital to emerging countries was significantly reduced. Given that, the macroeconomic policy of the new authorities decided to use as a tool to reduce the aggregate expenditure of the economy, a violent rise in short-term interest rates, in order to avoid an overvaluation of the exchange rate.

From a neoliberal point of view, it was suggested that a greater exchange rate flexibility would reduce the effectiveness of monetary policy and emphasized the negative effect of the real appreciation of the peso on the development of the export sector (Valdez, Prieto and Soto, 1998), and that argument itself, appeared as a good reason to discourage very pronounced and temporary assessments.

Contrary to this approach, the authorities played to keep the nominal exchange rate as fixed as possible, thus protecting the large indebted economic groups in dollars and leading the country to a crisis of magnitude. Exports fell by 28%, the deficit in the trade balance reached $ 2,500 million dollars per year, the current account deficit reached 5% of GDP, interest rates rose from 9% to 19% per year and GDP fell to -15% in 1999.

It seemed in those years that the positions had been reversed in relation to those that the two wings of the Chilean economists had sustained in the crisis of 1982. The strict neoliberals proposed to let the exchange rate float and not play by rigid modalities. This

27 Between 1996-1997, however, the BCCH implemented a mobile band to fix the exchange rate. In fact, it held an almost fixed nominal price for the dollar, which, as expected, made it possible for the Asian crisis to find Chile with a certain rate. of significantly delayed change (French-Davis, op. cit.).

produced a real revaluation of the Chilean currency. Progressives, on the other hand, played by a fixed exchange rate, adjusting the economy through the real sector, raising the short-term interest rate. The big economic groups supported this last position that clearly benefited them and that was the end of the neoliberal fundamentalist proposals, the neo-liberal line of the Washington Consensus had been imposed, which would soon be defended by the IMF.

Above all, at the international level the orthodox World Bank insisted on defending the validity of their proposals that had questioned the effectiveness of capital control policies (Claessens, Dooley and Warner, 1995); however, the ex post studies carried out in Chile on the impact of capital control implemented in said period Agosín and Ffrench-Davis, 2001, De Gregorio et al, 2000, Edwards, 1999, Gallego et al, 2002, Le Fort and Lehman, 2000) conclude that these controls modified the structure of maturity flow of capital that entered Chile, reducing the weight of short-term capital.

Additionally, the same studies acknowledge that the reserve managed to maintain a differential between the eternal interest rates and the internal interest rates that left space for monetary policy action. In general, these studies were not questioned in their conclusions neither by the WB nor by the IMF.

Despite this, the neoliberal policy mix that adjusted the economy from the real sector while restricting the opening of the capital market did not seem to work. The country entered a strong recessive crisis, which R. Dornbusch humorously named "The Massad recession".[28] In addition, the same studies acknowledge that, despite these measures, during the years 1997 and 1998, Chile fell into a deep economic crisis whose effects were felt until the end of that decade and marked the end of the golden period of the Chilean economy and its impressive growth rates.

This proved, in our opinion, the error of having privileged the maintenance of the exchange rate coupled with a policy of capital control. It is useful to implement a policy that avoids the excessive expansion of aggregate national demand in times of crisis that require containment. When these measures are accompanied by interventions on the exchange rate that strengthen the revaluation of the peso (deepening the balance

28 Carlos Massad, PhD of the University of Chicago, one of the leading Christian Democratic economists in the country and holder of impeccable democratic credentials, was at that time the president of the Central Bank, so Professor Dornbusch decided to baptize with his name the self-inflicted recession in which Chile fell in those years.

crisis commercial) and increases in the short-term interest rate that more than adjust spending induce a recession that could have been perfectly avoidable, just as Chile avoided the "Tequila" crisis, which almost did not generate any effects on its economy.

From this point of view, the controls showed rather to be a subject linked to the area of efficient macroeconomic management in times of crisis, without being part of a global intervention that broke with neoliberal orthodoxy, much less produced an epistemological rupture in the economists who led the country with the neoliberal view seen as a specific economic theory that proposes a global understanding of economic dynamics. These measures were undoubtedly contradictory with the neoliberal fundamentalist approach that wanted to accelerate the financial opening, based on a vision anchored in conceptual principles that assumed, without a mediation based on the peculiarities of the conjuncture, the one that "more freedom" for all the actors economic was better than "less freedom", both for the operation of an internal market, and for that of international markets, increasingly complex and endowed with extreme asymmetries, to which globalization allowed to expand its effects far more than borders national.

Despite the relatively harmless nature of the introduction of certain capital controls in the Chilean case, this was an element that contributed to the changes in the outlook that occurred in the IMF and the WB in the following years. Ten years later, the same IMF, in its electronic bulletin of February 19, 2010, published the article "Capital Inflows: The Role of Controls", in which it describes the circumstances in which, in its opinion, the control of the Capital inflows into emerging market economies can be a useful tool to lessen the impacts on the local macro- economy of a sudden escalation of these capital inflows. From this, the IMF officially abandoned its old perspective, which saw these controls as an alteration to the correct allocation of resources of any economy.

However, deducing that the adoption of the aforementioned capital controls should be viewed as a break from the neoliberal program would be an exaggeration. These measures fit without major difficulty within the neoliberal non-fundamentalist program promoted by the Washington Consensus through the support of the IMF. If one thought the opposite, and believed that the implementation of rates fit short-term capital is an act of radical break with the neoliberal model, it should then be concluded that there is no neoliberalism in the world (except in the heads of a few academic defenders of the Austrian school). A point of view that has been explicitly defended by authors such

as J. Williamson and P.P. Kuczsinky (2003); S. Edwards (2010), K. Schmidt-Hebel (2006); V. Corbo et al (2005) and R. Caballero (2007), among others.

Very much in line with neoliberal orthodoxy, the Chilean economic authorities assumed that the total financial opening of the economy should be implemented only after the opening of the real sector was consolidated and a new economic institutionalization solidified, such as the one proposed from the neoliberal perspective. Then, as the first stage of the process was not mature, financial opening could be postponed or reduced, temporarily introducing capital control methods. Even more so if those restrictions were applied jointly to a way of administration of the crisis attached to the neoliberal orthodoxy that favours a fixed (or semi-fixed) exchange rate coupled with a rise in interest rates to be induced by the State, the whole of the package can hardly be defined as one of rupture with neoliberalism.

Following the recommendations of the IMF, Chile applied capital controls ineffectively only during the period 1991-1998; however, once the effects of external shocks had passed, Chile eliminated these restrictions on capital movements and that is the situation that remains today, twenty years later.

2.4. The role of "Founding Fathers" of Neoliberalism in Legitimation and Consolidation of the Chilean Model

An important part of the reputation of the Chilean Model is based on the support that several prominent neoliberal authors have given to it in academic literature. The 1976 Nobel laureate Milton Friedman was undoubtedly the most important. His ideas served in Chile as the intellectual basis for the denationalisation, privatisation, and subscription of international free trade agreements that make up the heart of this model. In his view, a military dictatorship was not per se a desirable element, but he believed that, in the Chilean case, an authoritarian regime could be very useful for depoliticising the economy and separating it from the State in order to eliminate the pressures that some interest groups might exert (Friedman, 1975).

Such support gave to the Chilean model a paradigmatic characteristic fuelling the successive adoption of public policies analogous to the Chilean ones in USA and in the most important European countries. Because of the implementation in Chile, from 1973 onwards, of the neoliberal policies supported by Milton Friedman, the

GDP fell initially by 12%, the unemployment rate grew to 16%, and the value of exports dropped by 40% (Valenzuela, 1978). Nevertheless, from 1977 onwards, the system began to strengthen, with positive figures in all areas, with the exception of the high rate of unemployment that towards the beginning of the 1980s, amounted to 22% (BCCH, 2001), mainly due to the massive lay-offs of workers in privatised companies and public institutions. Given these positive outcomes, Friedman coined the expression "the Chilean Miracle"[29] to describe the results of its recommendations.

The above information should not lead us to conclude that the Chilean Model was a creation of Friedman or other American Neoliberal economists.[30] Friedman and another prestigious Chicago scholar, Friederich von Hayek (Nobel Prize in Economics, 1974)[31], played an important and inspirational role for their students. However, their real role was essentially one of the legitimisations of their pupil's proposals within Pinochet's

29 There is enough evidence, including the testimony of Friedman himself, that proves the crucial role played by a group of about twenty-five former Chilean graduate students from the University of Chicago (who became known as "The Chicago Boys") in the design and implementation of such a model (Silva 1992; Montecinos, 1998; Soto; 2012a). Evaluating the empirical experience of their students, Milton Friedman proclaimed that the market-driven policies of the Chilean military dictatorship had produced "an economic miracle". He together with F. Hayek, H. Harberger, G. Stigler and other senior Chicago economists, played a role of crucial importance in the orientation of the political economics of such a regime (http://www.elcato.org/milton-friedman-y-sus-recomendaciones-chile). Friedman was not alone in this effort. The reputed neoclassical Harvard macroeconomist Robert Barro (1994) also asserted that the Pinochet regime was *"an autocracy that had expanded economic freedoms generating tendencies to be more democratic" remarking* Chile's "*outstanding performance derived from the free-market reforms instituted by … Pinochet" (Barro, 2000)*. Even Nobel laureate Joseph Stiglitz (2002a, 2002b), a strong critic of the Chicago School, described Chile as an exception to the failure of unregulated free markets and free trade policies in developing nations.

30 See: Friedman, http://www.youtube.com/watch?v=dzgMNLtLJ2k).

31 In words of F. Hayek (El Mercurio interview, April, 12, 1981): "*I would say that, as long-term institutions, I am totally against dictatorships. But, a dictatorship may be a necessary system for a transitional period. At times, it is necessary for a country to have, for a time, some form or other of dictatorial power. As you will understand, it is possible for a dictator to govern in a liberal way and it is possible for a democracy to govern with a total lack of liberalism. Personally, I prefer a liberal dictator to democratic government lacking liberalism. My personal impression — and this is valid for South America — is that in Chile, for example, we will witness a transition from a dictatorial government to a liberal government. During this transition, it may be necessary to maintain certain dictatorial powers, not as something permanent, but as a temporary arrangement leading to a liberal dictatorship, not a democratic Government where all liberalism is absent".* These points of view were widely diffused during the regional meeting of the Mont-Pellerin Society (1981) that took place in Viña del Mar, Chile, with extensive assistance from the Chilean economic elite.

technocracy and the Chilean economic elite (De Castro in: Soto, 2012b:83), who initially had only offered qualified support of the neoliberal proposals.

The Chilean reforms from 1973 were also the first example of the implementation of a neoliberal reform programme, which, additionally, reversed a national process of transition to socialism. This process had the aim of evolving a model of radical capitalism, which constituted a unique experience at this time. The influence of the Chilean experience on subsequent global processes of reform and economic liberalisation is undeniable. Although the governments of neoliberal orientation in Europe and the US have not experienced the brutality that marked the Chilean dictatorship, and do not intend to replicate its political institutions, the applied economic matrix was undoubtedly the same.[32]

Since its origin, the so-called Chilean Model tried to systematise and implement a strategy that followed strict notions that were only based on the assumptions of the neoliberal view of process development. At that time, during the mid-1970s, the neoliberal proposals lacked practical experience in this area and, speaking internationally, their proposals constituted only an academic hypothesis and the draft of a political programme.

The deployment of the Chilean Model changed that situation. The model was inaugurated with an ultra-orthodox emphasis. In its first phase, its several policy measures and tools were integrated with the neoliberal principles described above, which proposed that human well-being can best be obtained by liberating individual entrepreneurial inventiveness and skills within an institutional framework characterised by strong private property rights, free markets and free trade (Larner, 2000; Plant, 2009).[33]

32 A clear example of such differences can be traced in the correspondence exchanged, towards the end of the 1970s, between the U.K.-prime minister, Margaret Thatcher and Professor Friedrich von Hayek, referring to the international political applicability of the Chilean Model. Thatcher declared allegiance to its neoliberal economic principles, but considered it unacceptable to implement a UK-policy guided by these principles, using the tools and polity that characterised the Chilean dictatorship. (See: http://diego-sanchez-de-la-cruz.libremercado.com/2012/10/16/las-cartas-de-thatcher-hayek-y-friedman-ii/).

33 With the passing of the years, the neoliberal reforms have become a "commodity", generally dissociated from the dictatorial component that "dirtied" the Chilean experience. Given this, the international academic discussion has moved to the arena of the general measurement of the impact of openness and liberalisation on growth, inequality and poverty, and more abstractly to the opening and liberalisation impacts on the organisation of the markets, the flow of foreign investment and on the

Although originally the Chilean Model was realised in the context of the particularities of the Cold War (which characterised the late 20th century and was decisive in the fall of Allende's Government and its replacement by a military dictatorship), soon the model was projected far beyond this point. Therefore, it is worth differentiating its later manifestation from the different stages of its early development.
The first period of reforms (1973-90) conducive to the implementation of the model, were launched after the military coup of 1973, and were characterised by an initial stage (1973-1982) of the implementation of the neoliberal model in its purest and most ideological form, the neoliberal-monetarist approach (Ffrench Davis, 1982).[34]

Within this first period, it is also possible to differentiate a second and less orthodox stage (1982-1990), characterised by the implementation of a more pragmatic neoliberal economic programme, and designed to overcome the deep crisis that emerged during the early eighties.

It involved a series of public interventions, including tariff increases; "selective" export incentives, a more flexible exchange rate, stricter regulation of financial markets, and the take-over of collapsed private banks before privatising them again once their balance sheets were in order thanks to public subsidies to banks and debtors (Ffrench-Davis, op. cit.).[35]

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diffusion of technical progress.

34 The monetarists consider that control over the money supply should be the main mechanism for governments to moderate fluctuations in the national economy, contrary to the opinion of Keynes according to which both the fiscal and Monetary intervention could (and should) be used to tame the economic cycles. Monetarism, while still forming part of neoliberalism, is not identical to it. It is not a programme of laissez-faire based on disregard from the state. On the contrary, it is a government programme aimed at the control of economic volatility. The monetarist programme tended to arise, even in the Chilean case, more as an option for state intervention alternative to Keynesianism, than as an ideological alternative in the Hayek style. However, its inclination to the policies of automatic adjustment and its emphasis on controlling the money supply so that the quantity of money does not grow faster than GDP, was meant to ensure that the "right prices" would be able to induce the automatic adjustment of the remaining real variables of the economy. In Chile, this led to neoliberal economist to take on a more radical version of Austrian School, the monetarist approach, thought which led to the collapse of the economy in the course of 1982.

35 If we analyse the literature of the eighties, we can observe that the most important economic adversaries of "The Model" (eg., Meller, Foxley, Arellano or Cortázar), grouped in the "Corporation of Economic Research for Latin America" (Cieplan), never developed a clear differentiation between neoliberalism and monetarism, so that the bankruptcy of monetarism was associated by them with the virtual disappearance of neoliberalism in Latin America, a factor that explains their sudden adhesion to

This non-monetarist neoliberal approach allowed the economy to overcome the acute financial crisis that the country faced in 1982,[36] stabilizing average figures of GDP growth close to 8% a year. This recovery period provoked in some economists the idea that Chile was experiencing a "second miracle", through which these results may be projected to the long term, generating a quick convergence of growth between the Chilean economy and developed countries.[37]

2.5. Was there a Change on the Neoliberal Character of the "The Chilean Model" during the 90s?

A second and new period of openness and reforms started in 1990, with the return of democracy. From this year on, the Chilean economy faced the challenges of achieving a sustained high average economic growth while simultaneously dealing with the great "social debt"[38] accumulated during the dictatorship. Therefore, a new period of the economic model began in 1990 led by a centre-left coalition of Socialists and Christian Democrats (in Spanish: "*Concertación de Partidos por la Democracia*") whose presidential campaign political slogans for democratic government were "Change with stability" and "Growth with equity".

During this time, a new emphasis was introduced into the economic programme and some reforms of The Model were applied, including a weak enforcement of labour

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The Washington Consensus (TWC) at the end of that decade, declaring that TWC policies were not part of a Neoliberal programme

36 The crisis of 1982 was mainly caused by the revaluation of the Chilean peso, which came about because of the implementation of a fixed exchange rate, inspired by the "Monetary approach to balance of payments". That approach and the nonexistence of a bank regulatory framework caused a collapse of the Chilean banking system and a fall in GDP of 14.3%, creating an open unemployment rate of 23.7% and an annual inflation rate of 20.7% (Meller1984b).

37 In general, the supporters of the Neoliberal model who believe in this statement, adhered to the analytical framework, pioneered by Ben David (1990), and Barro and Sala-i-Martin (1990). They argue that Chile, as with all less developed economies who implement full trade openness and market liberalisation, must expect a strong presence of foreign direct investment that would boost technological learning processes, improve human capital and increase the domestic productivity of capital, all factors that would enhance the processes of "conditional convergence" among countries with similar characteristics.

38 Social debt is a concept supported by the idea that social rights should have priority over economic freedoms (Infante, 1993).

rights, limited tax reform and a less conservative macroeconomic policy, which assessed that macro-equilibriums were an essential condition to obtain growth with equity. However, as we will show throughout this thesis, these reforms were not enough by themselves for us to accept the assertion which maintains that because of these changes, The Chilean Model had been drastically modified and longer can continue being characterized as an economic model essentially neoliberal.

Having analysed the previous points, we have been able to show that the characterization of the Chilean model as neoliberal is a complex issue, linked to a national reality that is even more complex and does not accept trouble-free interpretations. We believe that the aforementioned definition cannot be approached from a perspective that pretends to disqualify the Chilean model a priori from any analysis, nor to proceed to characterize the Chilean model as neoliberal or non-neoliberal, only in function of the appearances of some of its more specific aspects. Nor would it be as well reasonable to characterize the Chilean model in terms of the extent to which the country approaches or departs from the recommendations of multilateral organizations, such as the IMF or the WB, whose policies some persons defined as "neoliberals" and others simply as "techniques" and strictly adhered to a "neutral economic logic" of a "positive nature".

2.6. The relevance of the Chilean experience

The relevance of the Chilean experience within the discussions related to core areas of economic development theory, is unrelated to the rank of this small country at a global level. The fact that the Chilean economy exhibits one of the longest, consistent and apparently successful periods of implementation of public policies usually associated with the neoliberal approach, is a reason that might explain why this country has become a crucial example, widely used in the political and academic debate worldwide (Weyland, 2006).

On the other hand, the presence of an extended period of this kind of policy implementation has enabled the systematisation of the Chilean experience within a formalised development model. The scope of this model was not only national. In fact, its supporters consider it open to imitation and replication elsewhere, as they estimate its implementation has produced positive results.

Along these lines, specifically from 1990 onwards, the Chilean Model has produced an apparently successful combination of growth and poverty reduction. It has inspired several authors (Edwards 1996; Caballero and Harmour, 2000; Buchi, 2006; Cardoso 2009) to refer to it as a positive paradigm worth imitating, since it is assumed that its implementation would demonstrate the feasibility of a positive impact of the globalisation processes in a developing economy.[39]

This popularity does not constitute a minor phenomenon in the American continent. When, on the second leg of his Latin American tour 2011, US President Barack Obama arrived in Santiago (March 21 2011), he declared to the Chilean newspaper *El Mercurio* that he had picked Chile as one of his three stops because, the country was an example to other nations. *"The Chilean experience, and more particularly its successful democratic transition and sustained economic growth, is a model for the region and the world and it is also a powerful example of how the opportunities of today can and must be seized".*

In Latin America, it is not only the former President of Brazil, Fernando Cardoso, who has defined Chile as a model to follow (Cardoso y Foxley, 2010). The current President of Colombia (2016), Juan Manuel Santos, has also described as "special" and "strategic" his country's relations with Chile, reaffirming that Colombia wished "to copy the Chilean development model" because, he said, "the indicators show that is the most successful of Latin America" (El Mercurio, August 11 of 2011).

A similar position seems to be gaining ground in Peru, where prominent Peruvian academics argue that, within Latin America, the Chilean Model is the best reference for their country.[40] Analogous lines of reasoning are frequently utilised in Mexico and some Central American countries, as well as by Paraguayan authorities and the Argentinian, Ecuadorian and Venezuelan right-wing political opposition.

These references to The Chilean Model as though it has remained unchanged from 1973 until 1990, have muddied the discussion, given that there is not a clear consensus in relation to whether this "Model" maintains its essential features or these were replaced after 1990. The discussions and polemics about the neoliberal character of the second period of implementation of this economic programme have been strongly linked

39 See: J. Sachs 2015, http://www.cnnchile.com/noticia/2015/06/16/jeffrey-sachs-la-incertidumbre-ha-hecho-que-el-sector-privado-baje-su-inversion

40 See: http://perueconomico.com/ediciones/31-2009-sep/articulos/346--el-Peru-sigue-el-modelo-Chileno

to discussions about whether the Chilean Model has actually led the country down a path of real development, debates that have extended themselves beyond Chile´s borders (Weyland, Madrid and Hunter, eds., 2010; Cameron and Herschberg, 2010).

Indeed, globally speaking, the analysis developed by academia and the political world about the practical results of both phases of the Chilean experience, as well as about the theoretical implications raised by them, has helped to identify different aspects of the development processes implemented in open economies that had not been adequately explored. In the same way, the evaluation of the economic performance of The Chilean Model also made it possible to elucidate specific relationships between markets and political institutions existing in the context of an opening economy (Jackson and Richard, 2006). For that reason, the core purpose of this research is related to the area of the under-explored institutional determinants of development processes in a small open economy.

Institutions define the conditions within which individuals relate to each other. These relationships are composed of expectations, roles, powers and rights, which are defined by the institutions. However, neoliberals believe that all formal norms of social interaction have to be established through the market. They also assert that when this is not possible, the focus should be on building markets or in allowing individuals not already integrated access to them.

Given our intention to falsificate the neoliberal hypothesis, our focus will be twofold. Firstly, we will analysis the relevance of relationships between trade openness and economic performance. Secondly, we will analyse the influence of institutional environment and institutions of governance (Williamson, 1996: 4-6), organised according to the neoliberal perspective.

In this sense, in contrast of the analysis by professor Williamson, who assumes the institutional environment as a given and focusing its analysis only in the institutions of governance, we will give greater importance to the identification of the features of the institutional environment. It is summed up in the essential rules of the game that have given form to the Chilean Model, an issue that constitute an essential element to our research. It is one of the crucial questions for our study to define: if the Model's original neoliberal character has been maintained over time, or if, after the return to democracy, the change of some of those rules has modified the character of this model. However, we think that, without examining on a more micro analytic level

the characteristic of Chilean institutions of governance, it would be very difficult to adequately answer this essential question.

In this area of appraisal lie the most significant controversies surrounding the heuristic validity of the lessons to be drawn from the Chilean experience. Understanding the role of the evolutionary process together with the role that institutions have played in shaping Chilean economic behaviour will be the core issue analysed in this study. This issue is related to the presence in the Chilean case, of a causal relationship between trade openness and market liberalisation, and development. In undertaking this task, we will focus our research on ***the analysis of the rules of the game and institutional arrangements that let us define the presence or otherwise of relationships between the specificity of Chilean institutions and the outcomes of the trade openness and market liberalisation process***.[41]

Trade openness and market liberalisation are not the only characteristics that define the neoliberal nature of a development strategy, although they are essential elements of it. A neoliberal strategy implemented in an economy that remains closed and regulated would be something of a contradiction, because all the other macro and micro interventions proposed by neoliberals can only be established upon a process of trade and financial openness, followed by internal market liberalisation openness has been solidly installed (Broner and Ventura, 2010). For that reason, based on the findings associated with our research, as a secondary interest we will assess the levels of consistency of the neoliberal predictions associated with the implementation of the two quoted phases of the Chilean development model (1973-1989 and 1990-2009). However, we will focus our main interest on the second phase.

Finally, yet importantly, we intend to gauge the successes or failures in the implementation of this model, firstly regarding the maintenance or amendments to the grounds on which the model is based (the so-called rules of the game or institutional environment) (North, 1990). Then, we will focus on the characteristics of the institutions of governance, emphasising analysis of those institutions that clearly present relevant degrees of dependence from the big rules of the game inherited from the dictatorship.

41 41 We understand as a "rule of the game" (or institutions), systems of established and embedded social rules that structure social interactions (Hodgson; 2006), and by "institutional arrangements" the specific guidelines designed by economic agents to facilitate private exchanges (Williamson, 1996).

Given the issues outlined above, the research and evaluation of the Chilean Model does not seem easy to detach from the analysis of the harsh controversies that have surrounded its development. Nevertheless, we are not referring only to the local criticism. In some ways, from 1973 onwards, political and academic discussions surrounding the Chilean experience of trade openness and market liberalisation have expressed a tension between the most important theoretical models and assumptions about the behaviour of open economies contending in the international environment.

2.7. After Forty Years of Reforms: Is Chile Becoming a Developed Country?

Although the Chilean economy towards the end of the sixties was already one of the six most important in Latin American, it was far from approaching the role that it subsequently had in the region. During the period 1976 to 2009, Chilean trade openness was implemented at a deeper level than in any other Latin American or Caribbean country (see Figure 2.1). During the dictatorship period, Chilean trade policy was based on unilateral reforms, supplemented by multilateral commitments. However, since 1990, Chile's trade relations have become increasingly focused on the negotiation of bilateral trade agreements, showing a clear preference for concluding free-trade agreements that do not inhibit its own freedom to undertake further unilateral reforms. Because of this process, both an escalation in the participation of Chilean exports in international markets as well a reduction of national transport and communication costs was achieved, followed by a reduction in customs and legal impediments that limited the cross-border exchange of products, services, people, information and financial resources.

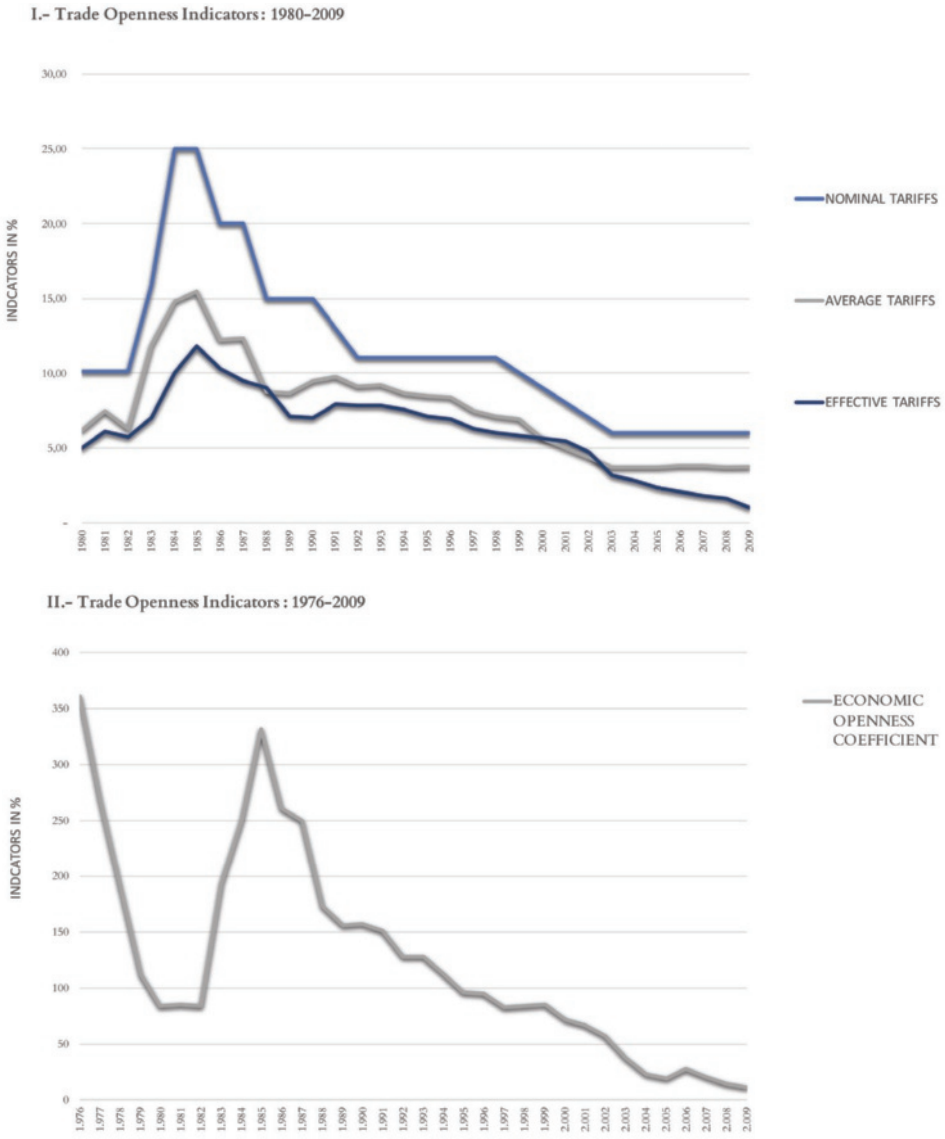

Figure 2.1 Trade Openness Indicators. Source: Author´s elaboration based on data from: BCCH, SNA, Ministry of Finances-DIPRES.

Whether the degree/level of opening is measured using the evolution of; nominal tariffs, average tariffs, effective tariffs or even if an Economic Openness coefficient is used (such as:(X + M) / GDP), the results remain very similar. The reduction of tariffs in the Chilean economy has operated in such a sustained and uniform way that, in an

extremely regular manner, the protection levels tend towards zero, regardless of the indicator used to estimate it.[42]

The structural reform processes associated to this full trade openness, have been associated with neoliberal theories that have already been in place for almost forty years now and their results seem to be remarkable in some areas.

The Chilean economy, compared to any other country in the Latin American region, exhibits among 1990–2009, higher levels of competitiveness, economic freedom, financial development, economic growth and human development.[43] In terms of foreign investment, in 2012 Chile attracted almost 28% of all the investments in Latin America with $ 30.323 million, while in the same year Chile became the second largest economy in Latin America in terms of reception and export of capital, and the first in the region in relation to its GDP per capita.

Some authors have identified these outcomes as clear examples of the success of the implementation of the Chilean Model, specifically focusing on the fact that Chile seems to be the only country in Latin America that, in the near future, has the potential to achieve the status of a developed country.

One core hypothesis formulated by academics who advocate for the Chilean Model was that trade opening, GDP and productivity convergence with more developed economies should be produced through the development of competitiveness engendered by openness and markets liberalisation.[44]

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42 In January 2009, there were three Chilean ad valorem tariff rates to imports: 0,6% per cent and 12.5 per cent. The most common rate was 6 per cent, which applied to 99.3 per cent of tariff lines, followed by 0 per cent (0.5 per cent of tariff lines) and 12.5 per cent (0.2 per cent of tariff lines).

43 The Human Development Report of the United Nations Development Program (UNDP, 2013), estimates that Chile is the country with the highest Human Development Index (HDI), in Latin America: 0,819 "Very High" in 2011), Chile obtained in 2013 the 40th place worldwide, only beaten by the US and Canada in the Americas. Recorded Chilean life expectancy is 79 years, infant mortality 8% and the illiteracy rate is only 2.4 %. The year 2013 marks the first time that Chile has surpassed a developed OECD country in the index, receiving a better evaluation than Portugal, ranked three spots below Chile at number 43.

44 A more extensive analysis of the theory of convergence and its empiric implications in the Chilean case will be developed in chapter 3 of this thesis.

In fact, if these two elements were to produce an improvement in competitiveness and, subsequently, create a growth dynamic that would allow Chile to converge with more developed countries, this would prove that the Chilean Model and its economic growth policies were successful in their aims. Obtaining this competitiveness-target will depend, in the first place, on a country's capacity to produce and sell its products in international markets (OECD, 2005). Furthermore, the development of competitiveness is an extremely complex issue, not reducible only to this specific factor.

If it is true that a country is competitive to the extent that its firms are able to compete successfully in the global economy, it has also been suggested that it additionally requires the generation of high and rising wages and the provision of an adequate living standard for the average citizen and a sustainable political framework. This means that competitiveness rests on the long-term production of a location as a place to do economy more efficient and, more specifically, improve the productivity of firms and workers, and the country´s economic aptitude to reach levels of high participation by working-age citizens in the workforce (Porter, 2011a, 2011b). Unfortunately, this process of building capacity in both workers and firms, as we will show in the course of the following chapters of this thesis, seems to be far from consolidated in Chile.

In fact, the expected results do not seem to have been achieved and Chilean institutional structures, which should have accompanied this process, do not appear to have reached (Kay, 2007) at least at the level which some orthodoxes analsys allege that they have (e.g. Leipzinger and Perry, 1999; World Bank, 199, 2002, 2013). Moreover, has been reported even by several studies of neoliberal inspiration (Alvarez y Fuentes, 2003, Larraín and Schmidt-Hebel, 2006; Fuentes 2011) and by other analysts (Kay, 1989; Ffrench-Davis, 2013) which criticize the neoliberal diagnosis, considering that, beside Chile´s trade openness and market´s liberalization has been present decline in multifactor and average labour productivity.

These scenarios constitute a serious problem that casts doubt on the route by which Chile is trying to achieve development. However, it is not desirable to analyse the empirical problems related to the eventual achievements or difficulties of the Chilean Model, without previously defining the positions of contending theoretical frameworks associated with the evaluation of this model.

2.8. Trade Openness, Market Liberalisation and Development: The Theoretical Debate

In keeping with neoliberal views, one of the key elements of the implementation of the Chilean Model was its unrestricted trade liberalisation process. The expected effect of this kind of total openness was to promote the competitiveness of markets, the development of growth and productivity, and a better allocation of resources. Within the Chilean model, market liberalisation followed by trade and financial openness were conceptualised as indispensable elements that must accompany the model´s implementation. However, without opening the economy to foreign trade, these decisions would lack sense. In the neoliberal discourse, trade openness and market liberalisation play a role of such importance that not only the economic performance, but the freedom of citizens, would depend on it. (Friedman, 1962; Lawton and A. Barkle, 2005)

Disagreements about empirical evaluation of trade openness and market liberalisation fallouts are not only visible in Chile. If we briefly review contemporary literature about the link between these variables and economic growth, it is also possible to establish a wide range of theoretical discrepancies between different worldwide schools of economic thought.

Much of the debate has focused on a crucial problem (Krugman, 1987, 1990; Dollar, 1992): Does trade liberalisation have a positive effect on economic growth?

Some empirical studies have identified a positive link between a country's rate of economic growth and its openness to international trade, showing that countries that opted for liberalisation programmes have improved their export performance (Weiss, 1992; Joshi and Little, 1996; Helleiner, 1994; Bleaney, 1999; Frankel and Romer, 1999; Ahmed, 2000; Bhagwati and Srinivasan, 2001 and Dollar and Kraay, 2001). Conversely, other studies have found little evidence of a relationship between trade liberalisation and economic growth, failing to demonstrate this link (UNCTAD, 1989; Agosín, 1991; Levine and Renelt, 1992; Clarke and Kirkpatrick, 1992; Greenaway and Sapsford, 1994; Shafaedin, 1994; Rodrik, 1996; Rodriguez and Rodrik, 1999; Rodriguez, 2006). However, these contradictory findings do not appear to correspond to econometric techniques or databases used by each author, but rather to the different theoretical and methodological approaches associated with each one of these studies.

In the Latin American context, controversies about the real impact of economic liberalisation on growth are linked to those issues, which have a long tradition and a wide scope. Three large schools have dominated the region in terms of the study of relationships between economic growth and trade liberalisation: the Latin American Structuralism School, the Neoclassical School and the New Endogenous Growth Theory.

2.8.1. The Economic Theory of Latin American Structuralism.

The structuralist model developed by the Economic Commission for Latin America and the Caribbean, (ECLAC), since the 1950s (Prebisch, 1951; Muñoz, 1974; Rodriguez, 1980; Prebisch, 1986), was characterised by its emphasis on the relevance of "structures". These were considered as a key factor in understanding the development process given the influence of heterogeneous economic structures on sectorial and global evolution in developing economies.[45] This structuralist analysis questioned the neoclassical notion of markets that prevailed before the Second World War, which tended to view them as capable of self-regulating and producing situations of stable equilibrium. ECLAC proposed instead a view of markets as a quantitative expression of the power of the contracting parties, at a national and international level. The influence of Keynesian thinking and the European historicist and institutional schools were instrumental in the early years of ECLAC´s formulation of ideas. National industrialisation projects were conceived as closely associated with the same issues established by Keynesianism in the industrialised countries throughout the three decades that followed the end of the Second World War. (Domar, 1946).

At this time, the political and social climate was permeated by the idea that it was possible to adopt national and international strategies for growth, industrialisation and social progress. ECLAC´s view was that if a different process and style of development could be promoted as an alternative to the status-quo, it would change the power

45 The Latin American economic structuralism has usually been interpreted as a by-product of the classic French structuralism of Claude Lévi-Strauss and others, without careful examination of this approach. The Latin American structuralist methodology was formed between the 1950s and 1970s, and within that period, perhaps the most important thinker within ECLAC that could be associated with this trend was Celso Furtado. Influenced by both C. Lévi-Strauss's and F. Braudel, Furtado's suggestion was that a combination of structure and history based on the use of economic models to interpret successive historical structures, associated with the development of the notion of creativity, be used as a link between structures and processes. It differed in some important aspects from the "historical structural method" usually associated with other Latin American authors such as Cardoso & Faletto (1969) and Sunkel y Paz (1970), built on existentialism and dialectics (Boianovsky, 2014).

structure of social systems and these changes would be reflected in the relative prices predominant in the economies (Di Filippo, 2009). ECLAC´s approach concentrated on the study of long-term structural changes and on the identification of bottlenecks and rigidities typical of developing countries that should be dealt with by the State´s development strategies, aimed at substantially changing the existing economic structures (Meier and Seers, 1984).

To ECLAC, the ideas of economic development and structural change were closely associated. The development process was seen as one of the reallocation of labour and capital from the low productivity sectors to the high productivity ones.[46]

From this perspective, it was assumed that the manufacturing sector was the one that would stimulate the productivity increases required for development, generating spill-overs, linkages (forward and backward) and pecuniary and technological externalities which, it was thought, would be associated with increasing returns to scale (Rodríguez, 1980).

The vision of Latin American development originally postulated by ECLAC was linked to a mix of industrialisation and expansion of regional markets (Kay 1989). However, this goal was associated with a gradual process of the formation of a Latin American Common Market and not to unrestricted trade openness and market liberalisation. In their view, economic integration had as a fundamental condition the deployment of a national process of industrialisation. ECLAC believed that a Latin American Common Market could only be built on that basis.

This proposal was suggested by ECLAC in 1959:"… *The common market isn't really related to these (pre-existent) activities, such as the ones that should develop from now onwards in response to the demands of economic growth. We are mentioning industries that have yet to be developed, or even more, that are in an incipient stage of development*

46 From this perspective, the necessary challenges to resolve it do not rest only on the mere accumulation of factors of production. First of all, ECLAC estimated that the concentration of technological progress had created a differentiation of productivity, inter and intra-industry, that went beyond the mere existence of a modern and a backward sector in the economy. This phenomenon was defined by ECLAC as: "structural heterogeneity" and was argued that, at a micro level, its presence was a complex issue that deserved a high level of attention given that in implementation of developmental policies there was no sound application of unique solutions to economic sectors highly differentiated in terms of productivity and size of the firms.

and from which it will be possible bring about with certain smoothness the reduction or elimination of tariffs that the common market building pre-supposes". (ECLAC, 1959:3-4).

On the other hand, ECLAC´s thoughts not only emphasised strategies divergent to those of unilateral trade openness and market liberalisation, but which also promoted a strategy strongly focused on the role of the State. At a macro level, ECLAC´s view stressed the presence of cross-sectorial complementarities required in order that the expansion of sectors occurs more or less simultaneously. The development of none of these was independently viable and the technological requirements, in turn, implied that the required investments were very high (Cimoli et al., 2005). Thus, the role of State appears to be highly relevant. From this situation, one of the most debated of ECLAC´s proposals in the Chilean context arises: the question of the role of State as the most important agent in charge of solving the structural problems of the coordination of investment decisions among actors.

Within the policies of structural changes proposed by ECLAC it is assumed that the only ones that possess viability are those implemented by the State as a comprehensive plan and not through the isolated actions of other economic actors. These kinds of State actions were visualized by ECLAC as more relevant than trade openness and market liberalisation. Additionally, they were visualised as necessarily immersed in a national strategy (defined top-bottom) focused on the promotion of structural changes, including the gradual transformation of the external insertion pattern (through promotion of economic integration), and the transformation of the employment structure. (ECLAC, 1969).

In short, to ECLAC a unilateral trade openness and market liberalisation would be associated with a lack of investment in technological learning; a situation that produces a decrease in a nation's own technological capabilities and a diminishing share of the sectors' diffusers of knowledge in the productive fabric associated with a low productive specialisation. This lack of specialisation would be induced by openness, when economies become specialised in the production of primary goods whose income-elasticity is less than the elasticity of goods imported from these countries. Then, according to this view, the pace of technological change associated with openness would put recurrent pressure on to the trade balance´s deficit and subsequently lead to increasing structural heterogeneity and income concentration. Based on this analysis, the solution proposed by ECLAC is very different to the proposal of radical trade openness and market liberalisation that seek that a globalised relative prices system defines the allocation

of resources. This task, in ECLAC view, should be assigned to the State rather than to market dynamics, since the State is the only economic agent capable of boosting strategies that lead to the overcoming of the structural heterogeneity in the peripheral economies and the boosting of its development process.

Many of the analysis originally developed by ECLAC, at least in the specific ways that they were originally formulated, have lost authority with running of the time the questioning of ECLAC´s thought has come from two sources. The first is associated with the criticism received from the influential new exponents of neoliberal-neoclassical thinking and the second one with the indisputable fact that since the eighties, not only Chile but also the bulk of Latin American countries, have opted for models of development far from ECLAC´s recommendations.[47]

The result of these critiques was a strong decline in the influence of ECLAC´s views in Latin America (Hodara, 1995). First under the neoclassical theoretical offensive that led to the installation within ECLAC of an approach self-defined as "Neo-structuralist" (Sunkel y Zuleta, 1990; Sunkel, 1991). After that, due to their relative isolation from the new public policies that the majority of Latin American governments used to explore new roads of development, distinct from those proposed by ECLAC.

Given that the thinking of ECLAC had been developed as critical to classic-monetarism, for a long time it benefitted from the predominantly Keynesian orientation of economic policies implemented by governments of the region and in many developed countries. However, as soon as anti-Keynesianism (led by the new-monetarism sponsored by neoliberal thinking) began to gain ground on both the regional and worldwide stage, the influence of ECLAC in the region declined substantially.

Additionally, ECLAC must face up to the challenge exerted by new institutional approaches. It has been observed that ECLAC's current thinking does not adequately

47 In words of ECLAC: *"As the evidence shows widely, (since the 191980s, in Latin America), the productive structure of large economies tends to be more diversified. ... the sum of exports and imports of goods and services as a proportion of GDP, is generally lower in these economies... the sum of exports and imports of goods and services as a percentage of GDP shows a major upswing over the three decades, pointed in particular in large economies that were relatively closed at the beginning of the 1980s. In all large economies and several medium-sized economies, the degree that foreign trade has an impact on GDP has doubled, at least in the three analysed decades. This has been result of conditionality's associated with financial support packages to deal with crises suffered by countries in the region between 1980 and 1995, as the adoption by countries of strategies of development that deliberately sought greater integration to the external markets." (ECLAC, 2013: 94),*

define at least two issues: the role of the political and economic institutions in which the dynamics of development processes rest, and the relation of both of them to the social agents that determine such processes (Kay, C. (1989); Boianovsky, (2014)).

The focus of ECLAC has always been defined, in its different nuances, by a definition of the role of the State as an agent that over-determines the characteristics of structures in which it is immersed. Therefore, ECLAC portrays the State as the only means of championing the development process, an approach in which "structures" are a concept very different to "institutions".

ECLAC view is placed so distant of the main institutional approaches that focus their interest on the links between social structure and agency (Hodgson 2004: 179-181, Fleetwood, 2008a, 2008b). In this way, ECLAC´s approach moved away from theories that visualise structures, at the same time, as instruments and as products of the process of reproduction of social practices (Giddens 1985), and from those that emphasise the need to analyse the micro-dynamics of institutions of governance (Williamson, 1991).

In ECLAC´s view, structures exert influence from the top and do not participate in the constitution of agents or social practices. For this reason, ECLAC´s approach did not adequately deal with the analysis either of agents of change, or of the definition of the rules of the game that produced the institutional structures which are enhancing the heterogeneity of the economies that they aspire to change.

In sum, in ECLAC´s vision, development depended ultimately on the State´s ability to induce technological progress, underestimating the role and endogenous capacities of other actors and what Giddens called "alternative interactions between agents and structures" (Giddens, 1985; 1998). Thus, in their view, the influence of the State and the public policies on the modes of organisation of the economic structures are not perceived as a process of conformation of institutions, rather a mechanism of determination of the economic agent's behaviour, motivated by the pressures, or signals, emanated from the actions of the State that leads the development process.[48]

Since the seventies, ECLAC´s paradigm has shown a declining influence, concerning a decrease in import substitution strategies resulting from their failure to incorporate

48 Of course, there are different versions of the Latin American structuralist approach, it being necessary to differentiate the ECLAC's Orthodox approach from versions of different Marxists trends associated with dependency theory and from the new neo-structuralist ECLAC´s approach.

into their analysis elements that would enable us to understand existing links between the State and the other agents of change.[49]

Criticisms coming from the right-wing side emphasise eventual mistakes in the valuation of the role that trade openness and market liberalisation and free markets must play. The structuralist idea that inflation is not a simple monetary phenomenon, but the result of real imbalances, manifested in an increase in the general level of prices, was also strongly criticised by them.

From the left-wing side, many critics estimated that ECLAC has been assimilated, in many areas, to neoclassical-neoliberal thought.[50]

Although proclaimed as an alternative to neoliberalism, Latin American neo-structuralism ended up sharing with the neoclassical approach (and sometimes with the neoliberal), many of its tenets and analysis (Hernández de Gante, Gimate-Welsh et al, 2010). The new thinking of ECLAC was adapted to the new times, placing their emphasis on promoting *"policies that seek to correct, complete, or promote the factors' markets - primarily the human capital (education policies), and technology (science, technology and innovation policies), as well as attending other institutional aspects that determine the environment in which enterprises are developed"* (Houni et al.; 1999).

As we will show below, ECLAC´s neo-structuralist approach shared many of the assumptions of the New Endogenous Growth Theory (NEGT), especially as the technology market had failures resulting from the mixed public-private status that the technical knowledge and information markets have. In addition, they have points in common, considering that, these failures led to an underinvestment in technology and justified a direct intervention by the State through horizontal and meso-economic policies. Further, the neo-structuralist approach did not criticise the fundamentals or the basic principles of adjustment policies. Their criticism was limited to judgements

49 A no less important element that explains the loss of influence of the ECLAC in Latin America was the location of its headquarters in Santiago de Chile. As Bielschowsky says (1998b:39): *"Between 1973 and 1989, the headquarters of ECLAC in Chile lost what had been until then one of its main assets, the convening power of Latin American intellectuals; economists, sociologists, technocrats and politicians from democratic and progressive tradition simply ceased to be able to or want to circulate in Chile".*

50 Authors like Leiva (2008) lambasted Eclac´s neo-structuralism for having discarded key tenets of the economic left in Latin America, particularly the centre-periphery model and the framing of development problems in the hemisphere, in the context of the capitalist world economy.

about the rate and extent of the adjustment and to denouncing their negative social consequences for Latin American countries. It was a critique of the way in which things were done and not of the fundamentals of neoliberal thought.

The neo-structuralism of ECLAC has tried (not always with success) to preserve what constituted the central nucleus of its original thinking, integrating some new analysis of structural heterogeneity and income´s concentration issues. Nevertheless, it has discontinued its use of other basic distinctions of old structuralism, i.e. the reference to classes or social groups in the study of inequalities in the distribution of income, and its implications for international trade.

Additionally, its analysis of the demand side is more prevalent now than in the speech of precursors, since they considered that the problems of Latin America were essentially based on the supply-side. In short, a careful examination of their neo-structuralism shows how, in its eagerness to compromise, it has incorporated essential neoclassical approaches and ignored others coming from classic structuralism.

2.8.2. The Orthodox Neoclassical Approach and its Neoliberal Drift.

The analysis of the problems linked to the economic heterogeneity and income concentration was not, however, the exclusive concern of structuralism. A long time ago, during the same period as ECLAC, some authors like Lewis (1954), had dealt with issues of productivity segmentation across sectors and sizes of firms from a neoclassical perspective, and brought the concept of dual economies into focus.

As Sachs (1997) widely describe, the link between the functional distribution of income and savings and growth is at the heart of the neoclassical growth model of Lewis and later of Solow. Beyond this initial recognition of the problems related to economic heterogeneity, the neoclassical theory was built on assumptions that greatly differed from the structuralist approach of ECLAC already described.

Throughout Latin America, from the seventies onwards, a great deal of theoretical and empirical work on economic growth, based on the neoclassical growth model, began to displace influence of other theories. The basis of this new approach was advanced

by Solow (1956) and Swan (1956),[51] and explained the growth of the product per capita because of exogenous technical changes.

This approach was consolidated into a model that came to be known as the model of Solow-Swan, which highlights the role of the expansion of the physical capital per worker to explain the main macroeconomic aspects of economic growth.

In it, the product per capita in the long term (in a steady-state) depends of the saving rate of the economy, which determines the stock of capital; while the production function depends upon the state of the technology. In a steady state, the growth rate of aggregate production depends on the rate of growth of the population and the rate of technological change and then the rate of growth of per capita output is visualised as independent of the rate of savings (investment), depending only on an exogenous technological change.

The Solow-Swan model features a unique and stable steady state, which will be achieved regardless of the initial conditions. In this model, given that technical progress spreads around the world, it is possible to predict that there will be the convergence of per capita growth rates, and even of per capita income levels.[52] Based on what this model predicts, those economies whose capital per capita is initially low (poor regions), will grow at rates higher than those economies where it is higher (rich regions).[53]

Subsequent to the publication of the pioneering Solow paper, the orthodox neoclassical approach was the main point of reference for theoretical discussions on the subject, so

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51 Originally, Solow (1956) advanced this approach. In its first meaning (known as absolute convergence), an implication of this hypothesis is that, in the long run, countries or regions should not only grow at the same rate, but also reach the same income per capita. The Solow model predicts an "absolute convergence" between countries of different levels of development. However, "conditional convergence" means that only after controlling for structural differences we will be able to observe the negative relationship between the initial level of GDP per worker and subsequent growth when lagging countries catch up with technological leaders. The paper of Swan (1956) was published ten months after the Solow paper, but in it, characteristics of technical progress are developed in a more detailed way than in the Solow one.

52 In its first meaning (known as "absolute convergence"), an implication of this hypothesis is that, in the long run, countries or regions should not only grow at the same rate, but also reach the same income per capita.

53 This "convergence hypothesis" was later developed and documented by Baumol (1986) and Barro and Sala-i-Martin (1995).

that ultimately this kind of analysis of economic growth soon became the dominant method of the economic theory (Jones, 1988:83).

In this orthodox neoclassical model, long run growth depends on the rate of technological progress, which the model takes for granted rather than explains. Then, based on this perspective, some neoclassical and neoliberal analysts would assume later that, given that trade openness and market liberalisation induce changes in relative prices, these would be the big factors that attract exogenous technical progress, generating new and better resources allocation processes that will propel the economic growth by improving economic efficiency.

As can be seen at Figure 2.1, from the point of view of orthodox neoclassical theory, and especially from the neoliberal point of view, changes in relative prices stimulated by trade openness and market liberalisation should not only result in changes in sectorial specialisation but also in substantial changes in global and sectorial productivity of the economy.

Within this view, the neoliberal interpretation of the development process gives to the economic openness a central role that should only bring benefits to domestic companies and to the country in general. In their perspective, competing with companies from other countries means that domestic enterprises must sell their products abroad and, simultaneously, defend their internal markets from foreign competition.

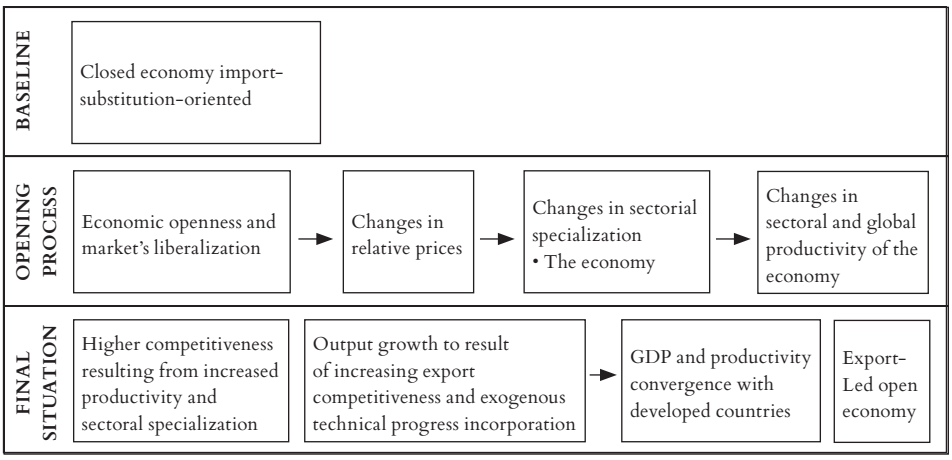

Chart 2.1 Neoclassical- neoliberal hypotesis: Impact of trade openness

To do this they ought to promote, among other strategies, a good price-quality correlation in their products so they are attractive to buyers.

To make this happen, companies must organise and strengthen themselves in the best possible way. The most sensible path should involve a mixture of the absorption of exogenous technologies, new machinery acquisition and a serious improvement of their management capabilities (assimilating international best practices) that allow them to produce with low costs.

By incorporating these exogenous sources of technical progress, the companies would become more efficient and competitive. From the perspective of this neoliberal drift of the orthodox neoclassical theory, the State and the companies should adapt themselves to the new context of an open economy, focusing on infrastructure enhancements, human capital improvements induced externally, and enabling the assimilation of foreign technologies. Consequently, all these actions would reduce the production, logistic and information costs to the economy.

In this analysis, development depends essentially upon changes of relative prices that allow the potential assimilation of exogenous technical progress, affecting the survival of different companies. These changes would result in the disappearance of those firms that fail to be internationally competitive (ceteris paribus the best international productive practices) with the new relative prices. At the same time these new prices would allow the development of firms that are better at managing their adaptation to this new context, facilitating an absorption of exogenous technologies that allows the economy to produce better goods and services, susceptible to demand from consumers both nationally and abroad. From this standpoint, the neoclassical-neoliberal public policies popularised because of the Chilean experience, spread widely across the Latin American region, tending to concentrate their goals in a single and simple formula: "make the prices right". They assumed that any sectorial policies or any attempt at industrial or economic promotion operating beyond the price system, emphasising the development of endogenous capacities, must be rejected and considered counterproductive for an adequate allocation of resources in the economy (Breton (2007)).

2.8.3. The Endogenous Growth Theory

Since the seventies, the previously described neoclassical and neoliberal analysis of intricate development problems played a hegemonic role worldwide. However, since

the second half of the 1980s, within the neoclassical thought, some growth models began to develop more consistent models than the old-fashioned proposal by Solow-Swan. These models, named the New-Endogenous-Growth-Theory (NEGT), emerge as critics of the old neoclassical explanations, understanding the technical change as an endogenous phenomenon and then abandoning tools like the neoclassical production function and the hypothesis of diminishing marginal returns of capital, which emphasised the role of exogenous factors. A synthesis of both hypotheses (New version of ECLAC theory and NEGT) is presented in Figure 2.2 below.[54]

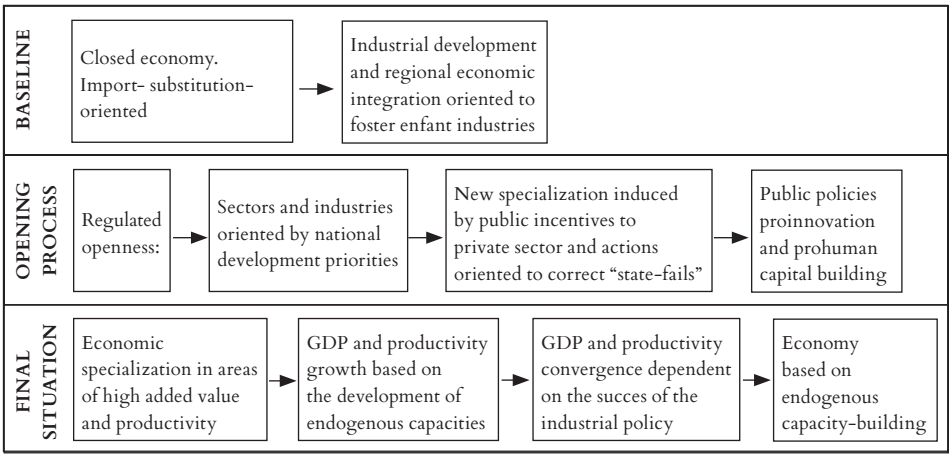

Chart 2.2 Eclac's structuralism and negt hypothesis: impact of trade openness.

The initial investigation upon which NEGT was founded was based on the work of Arrow (1962), Uzawa (1965) and Sidrauski (1967) and further developed by Romer (1986) and Lucas (1988). It began to incorporate new assumptions, hypotheses and factors, different to those considered by the orthodox neoclassical version. Subsequently, Rebelo (1991) proposed a simplified version, Sala I - Martin (1990) elaborated a survey and then a manual written with Barro (Barro and Sala-i-Martin, 2003 (1995), thus contributing to the dissemination of the new approach.

54 The endogenous or exogenous nature of the technological change refers to its source: endogenous change is internal to the national economy, being created by domestic private or public enterprise, while exogenous change is external, originating from foreign sources. The NEGT favoured explanations that replaced the exogenous growth (undetermined technical progress) variable by one whose growth´s determinant variables are included in the model itself.

Since then different versions of the NEGT have been published throughout the world, covering such diverse fields of research as infrastructure (Barro, 1988), innovation (Grossman and Helpman, 1990), development (Azariadis and Drazen, 1990), international trade (Krugman, 1990), demographics (Becker et al., 1990), creative destruction and endogenous growth (Aghion and Howitt, 1992; Aghion, and Durlauf, 2005; Aghion et al., 2008).

A common point in all these models[55] is their concern with a crucial problem of developing economies that had found no place in the previous analysis:[56] The investment in human capital that caused spill over effects on the economy, reducing the diminishing returns of capital accumulation (Benhabib and Spiegel, 2002; Erosa et al.; 2010).[57] While in the Solow-Swan type models, exogenous technological changes are considered to be unaffected by country integration to world trade, in the NEGT trade policy reforms are especially important and influence the long term economic growth of a country. For instance, Barro (1991) and Gundlach (1997), assess that countries which are more open tend to move faster towards their steady state growth path when compared with those that are following a protectionist trade regime. Other authors, like Gross and Helpman (1991) or Edwards (1992:33-40), stress that in smaller countries the role

55 In general, we can distinguish first and second-generation models within the NEGT (Cesaratto, 1999a, 1999b, 2009). The first ones (semi-endogenous models), are those inspired by the "learning by doing" of Arrow (1962), whose key idea is to eliminate from function of production the «not explained factor», so avoiding any source of diminishing returns from the productive factor. On second-generation models (fully endogenous models), the dominant idea is to integrate to the technical change of the Solow equation, the existing relationship between the rate of change in labour productivity and the choice of the society between present and future consumption. This choice obviously affects the productivity of the work through its impact on resources devoted to R&D, education and infrastructure.

56 Within this new perspective, authors like Stiglitz (1998), Chang, (2001,2002), Temple (2003, 2005), and Banerjee & Duflo (2005), have suggested that a better understanding of the growth and development process requires the explicit adoption of models that incorporate the presence of heterogeneity and market failures within economies. The relevance of these kind of issues for understanding income differentials across countries has been also established by several recent empirical papers (Chanda and Dalgaard, 2008; Córdoba and Verdier 2008; Restuccia, 2008, and Vollrath, 2008, 2009). Some of these approaches support the idea that the inefficiencies inherent in a dual or heterogeneous economy can explain over half of the observed variation in TFP at the country level. Temple and Wößmann (2006), assert that labour re-allocation has a significant influence on country-level growth rates, suggesting that aggregate productivity may be depressed by a factor misallocation to low productivity activities (agriculture or MSMEs: Micro, Small and Medium Enterprises).

57 Following to Romer (1989), we assume that human capital is the accumulation of effort devoted by an economy to schooling and training.

of trade openness and market liberalisation is crucial in fostering the absorption of exogenously produced innovations at a faster rate, a process less feasible in more closed economies. This means that, in their views, economies that are closed to international trade would grow more slowly than economies with a higher degree of openness.

One of the predictions of the NEGT is the absence of convergence of growth among countries, with the key finding that in market economies the State must intervene to accelerate capital accumulation and growth in the long term. Endogenous growth models are usually presented as a macro-dynamic version of the Walras general equilibrium, equipped with solid micro-economic foundations. This is associated with the NEGT's divergence from the old representation of the Solow-Swan model.

This model was incapable of explaining the original´s rise in GDP and productivity. NEGT thus allowed the identification of current technical progress and growth engines, using notions such as knowledge-based economy, externalities and increasing returns. Despite this, the key point that has lent a progressive aura to the NEGT has been its rehabilitation of the intervention of the State in the development process.[58] This has somehow created a bridge between neoclassical and heterodox economists. Despite the "charm" of NEGT derived from their view of the state role, within this theory the State is represented in a contradictory way as being at the same time both present and absent.

For instance, technically speaking, the models of Romer (1986, 1990), Lucas (1988) and Barro (1988), exhibit a below-optimal competitive equilibrium due to their decision to integrate externalities associated with knowledge and training or infrastructure. The State appears as a key element to justify and formulate proposals of public intervention in order to restore a Pareto-Optimal situation. Then, the NEGT recommended policies that operate through subsidies and lower taxes in favour of private actors that drive the engine of growth. However, at the same time, the State as institution or autonomous entity is absent in other areas.

The NEGT has exerted a highly seductive influence on the new generation of economists who arrived in the Chilean Government in 1990. The reason for this effect is perhaps linked to the fact that this theory explains the divergence between

58 For instance, ECLAC´s structuralism has declared certain sympathy for the NEGT based on their policy recommendations, regardless of disagreement with some of the neoclassical theoretical grounds in which they are founded.

paths of per capita GDP growth between countries and provides a new version of the Big-Push model of Rosenstein-Rodan (1961). However, this new vision is now equipped with multiple equilibriums, (Durlauf, and Johnson; 1995) that are focused on knowledge and some formalised Schumpeterian views about stochastic processes, developing a sort of "cognitive-capitalism-analysis" of "knowledge externalities" (Moulier-Boutang, 2012).

This new approach of endogenous growth has given rise to several recommendations regarding State intervention, and therefore it has fascinated Keynesians, Neo-Keynesians, Structuralist and Regulationist alike. Unfortunately, their models remain locked within the confines of the neoclassical programme and therefore face the same conceptual difficulties. The weakest points in the endogenous growth theory are very similar to the difficulties of the neo-structuralist ECLAC approach we have already analysed, and refer to their fragile characterisation of (for them) the main agent of development: The State.

These weaknesses in the NEGT are nothing but an extension inherited from neoclassical economic, theory that permeates the new theoretical framework. The State institution is viewed as unable to reach an optimal competitive balance, even though it is able to internalize the external effect of their actions. This approach has given rise to different interpretations, which leave open options for institutional forms to adopt in order to foster development processes. In sum, these new models of endogenous growth are not, however, neutral: their "endogenization" is ultimately a by-product of market forces and the role of the State, according to them, aims only to promote, enhance and mobilise the capacities of private actors. The neoclassical shortcomings of NEGT are more marked in some of the so-called 'neo-Schumpeterian' versions (Hanusch and Pyka, 2007: 1160-1170), which include the idea that technical change is "almost" exclusively led by market forces.[59]

The economists of post dictatorship governments unreservedly ascribed the problems of the economy and development that Chile faced to this new conceptualisation, but without using a strictly Schumpeterian perspective.
They do not make a distinction between the levels of micro - meso - macro policies to be used in each situation, as is traditional in Schumpeterian analysis (e.g. Holland, 1987; Zezza and Lambi, 2001; Dopfer, et al.; 2004; Dopfer, 2007). On the design of

59 The word 'almost' is justified in this instance by the role assigned by his approach to tax incentives to private R&D and education that would be the origin of endogenous technical progress.

public policies, they emphasised utilisation of a macroeconomic tools in a traditional way. In spite of this, they frequently define themselves as Neo-Schumpeterian, but from the early 90s starting to defend points of view, which were closer to the American Public Choice School (Buchanan, 1984, 1986; Tullock, 1967)[60] than Schumpeter was.

The novel treatment of these issues opened up the possibility, to the new economist in charge of the new post-dictatorship governments, of obtaining certain legitimacy within the dominant neoliberal economic mainstream, which controlled the domestic academic life. Without clear-cut strict neoliberal arguments, they justified certain new policies of State intervention, marking a clear break from the rhetoric that had prevailed during the period of military dictatorship.

We can separate the former four approaches into two groups, on one side neoliberal and orthodox neoclassical theories[61] and on the other side, ECLAC´s structuralism and NEGT (Hounie et al., 1999:64). However, it is still possible to differentiate a fourth group of emerging approaches to the issue under study, the Institutionalist.

2.8.4. The Institutional Approach: Why History Matters.

We can denominate this fourth group as "Institutionalist Analysis", a heterogeneous and in building methodological process whose approach to issues like which are addressed in our research, is extremely useful, and therefore we subscribe and will utilise.

As already stated, through our research we understand institutions as systems of established and embedded social rules that structure social interactions (Hodgson, 2006). In the Chilean case, this concept of institutions appears crucial to the analysis of issues related to different spheres of the action arena[62]: the political arena (e.g. analysis

60 Public Choice is the application of the Rational Choice model to non-market decision-making. In a more general sense, it has meant the application of economics to political science. That school combines the "homo economicus" assumption, under which individuals are seen as seeking to further their own self-interest, with an approach to collective action in which individual decisionmakers use the political process to further their self-interests (Tullock, 1965).

61 That segmentation in only two groups is also based on Chang (2003:41-60) who affirms that Neoliberalism was born out of an "*unholy alliance between neoclassical economics and Austrian-Libertarian tradition" (op. cit., page 4).*

62 When we refer to the concept "action arena", we are referring to the space of intersection of a set of physically possible actions, outcomes, take-ups, decision functions, information, and participant's

of electoral system and other constitutional issues), the socio-economic arena (e.g. definition of property rights and public policies), and the cultural arena (that governs the ideology and thought models).

Neoclassical economics tends to create a comprehensive theoretical system that emphasises rational choice and the mechanisms of allocation of resources based on the price system. From there, universal validity policy recommendations are extracted. On the contrary, institutional analysis, in its different versions, incorporates a theory of institutions into economics that, in several aspects, modifies or substitute neoclassical analysis, connecting theoretical and empirical research, in order to explore the role of institutions in fostering or blocking economic growth.

Within the institutional analysis has gained increasing popularity so-called New Institutional Economics (NIE), which for some authors is a mere extension of the neoclassical economy and for others a new approach that in many respects surpasses or replaces it.

Often the criticism that frequently surround the application of NIE' approach (e.g. Field, 1981; Dugger, 1988; Menard 2010), within the academic circles has been gaining strength the view that maintains that, from the NIE, also it is possible to understand institutions as inefficient rules of the game that despite that may emerge and survive (e.g. Rutherford 2001).

From that last view, NIE are tending to converge with the perspective of the old institutionalism that did not consider existing institutions as necessarily functioning to promote the social benefit-in fact, rather the opposite (Veblen, 1919). In both perspectives (old and new institutional economics), existing institutions, due both to the inertia inherent in any established scheme and to the defensive activities of vested interests, tended to become out of step with new technological means and with the economic issues and social problems they produced (Veblen, 1899).

Many different "institutionalisms" have flourished at various times and places within the social sciences and the discipline of economics but, in particular, in our research we ascribe to the perspective that stress the role of economics interest in the process of institution´s building, because from our perspective, institutions were more than

positions (Ostrom et al, 2006).

merely constraints on individual action, but embodied generally accepted ways of thinking and behaving.

Thus, institutions worked to mould the preferences and values of individuals brought up under their sway. However, we think that sequential set of institutional changes are defined by the historical and cultural features that characterize each specific process of institutional change. It is precisely in this sense, in which we analyse the vast institutional changes introduced by the neoliberal model in post-1973 Chile.

Our perspective it is so close to Veblen's perspective of growth process that considered institutional change and cultural growth as determined by the economic interest, is worth to say as a cumulative sequence of economic institutions stated in terms of the process itself (Veblen; op. cit). From that perspective, an institutional theory, like the formerly described, must be considered as framed in an evolutionary perspective. Then, perhaps the best denomination to our research framework must be "evolutionary" more than "neo-institutionalist". However, several elements of NIE approach were uses in our research.

The most important elements of NIE incorporated in our research are related to the two areas of institutional analysis.

The first one is the "institutional environment", a term related to macro level relationships that constrains the contractual arrangements and social agreements, governing the activities of any specific group of people pursuing a certain objective. The institutional environment consists of the comprehensive socio-economic context within which different institutional arrangements take place, constituting the background constraints, or 'rules of the game', that guide individuals' behaviour and micro-institutional arrangements. A good example of this environment are the constitutional rules of the modern State. (Williamson, 1996:327-328)

The second one, are the "institutional arrangements", a term used to mention the micro-level relationship between actors. Those arrangements may be referred to contracts, exchange goods, and different kinds of agreement between economic actors involving activities like exchange or coordination of goods, services or productive factors, design, operation and enforcing of such agreements demand the spending of resources and thus involve somehow redistributive aspects associated with the arrangements to be established between economic agents. (Williamson, 1996: 11-12).

If institutions influence the performance of national economies this means that, in the long run, the performance would be influenced mainly by the way in which their institutions evolve. For this reason, the institutional approach outlined in this research believes that the values, standards, laws, informal rules and conventions, and institutional arrangements that shape such institutions, must be considered not only as a product of the dialogue or interaction.

From this approach, all these factors must be also visualised as a product of interest´s divergence between different groups of a society being part of a historical process of continuous change and evolution based on such conflicts. In this sense, economic performance tends to be, from this view, a variable depending on history and social conflicts, and not just a technical by-product, emerging from an ahistorical context.

Consequently, assuming the institutional point of view, our approach is an historical one and does not presume that the same social and economic forces (and their associated "technical" proposals) will generate the same results, regardless of the place of application. On the contrary, it assumes that their effect would be mediated by the context and legacy forces of history (JIE; 2007).

Therefore, from that point it is assumed that, firstly, in every society the political institutions will be define the framework in which, secondly, the economic institutions built on them will be framed. This process tends to be framed into a long-term itinerary, and the duration of the Chilean experience (forty year) offers a superlative opportunity to analyse in depth the process of the design and operation of a neoliberal economic institutional structure. The extension and radicalism of Chilean process is what makes this case such a robust research topic, especially considering its strong paradigmatic character, given the aforementioned historical situations in which it has been developed.

From the analysis of the new Chilean neoliberal institutions, seem clear that they play a crucial role changing the cultural scraps and schema diffused thought the institutional and organizational environment built during the first decade of military dictatorship (1973-1983) and consolidated by the new political constitution of 1980. Then, using some elements of the already described taxonomy proposed by one of the most important neo-institutional thinkers O.E Williamson (1985,1991),[63] is possible to asses that during the analysed period (1990-2009), two factors have been extremely relevant:

63 We think that differentiation between "institutional environments" and "institutional arrangements" (understood as institutions of governance) are the more useful distinctions proposed by Williamson;

1. The permanency of a neoliberal institutional environment.
2. The building of a wide spectrum of institutional arrangements, which were breaded, consolidated and legitimated throughout the subscription of a "pact" amongst the political leaders of the new and the old regimen.

The first of these two factors, the institutional environment, is composed by the macro rules of the game that influence the whole transactions of the economy. It included a wide range of values, norms, constraints, conventions and specific rules, which, in the Chilean case were not a result of economic evolution. On the contrary, their genesis was characterized by presence of multiples authoritarian decisions that implied an extended use of violence from the State, some of them crystalized in formal rules of constitutional range and others in a heterogeneous group of arrangements.

That heavy institutional framework has limited possibility to build some institutional arrangements contradictories to neoliberal orthodoxy, but is not right and proper to assume, based on this fact, that neoliberal rules of the economic game are only a creation of Pinochet´s dictatorship. On the contrary, several of the core aspects of them were created or consolidated after 1990 by post dictatorship governments following TWC prescription.

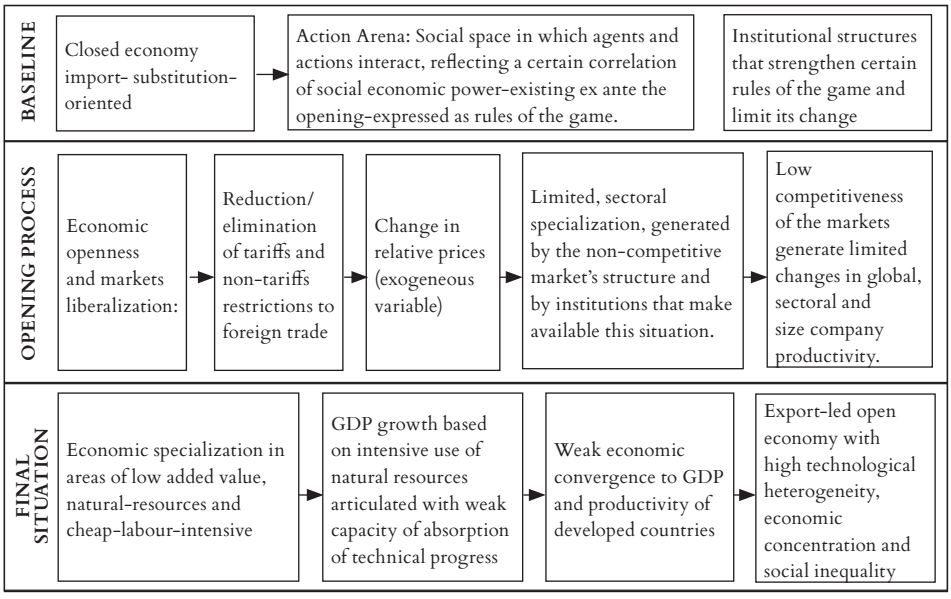

Chart 2.3 Institutional hypothesis: Impact of trade openness.

however, we do not share his view of "institutions of governance" as an evaluative outcome of the firm´s search of transaction cost minimization.

For the realisation of this type of institutional analysis of an economic process as complex as the Chilean one, we will use an approach coming from NIE, but we recognise that there are, between different institutional schools of various denominations, several shades and even major methodological differences that need to be taken into consideration.

Figure 2.3 reflects the mode through which the Institutionalist analysis (as a whole) displays the impact of processes of economic openness.

Nevertheless, presence of common approaches within institutional analysis there are important differences and we understand that institutional analysis is an eclectic movement collating different theories developed in several areas, which have a great size and diversity.[64] In spite of this, the different schools have at least three subjacent common elements, which let them share the hypothesis displayed at Figure 2.3:

1. The focus on distributional effects of institutions,
2. The presence of institutional explanations about formation of preferences, and
3. The focus on the building of institutions through a contingent and multi-causal analysis that frequently highlights the historical peculiarities.

Nonetheless, within institutional approach there are important differences between different schools. For same authors linked to New Institutional Economics (e.g. O.E. Williamson; 1996, 2000), market is viewed as a "state of nature" but, on the other, hand others authors conceived it as a "social construction". Some authors like Richardson (1972) and Dore (1983) argue convincingly that institutional arrangements not only exist in a sea of relations of market, but also are who constitute such relations. They argue which, in practice, firms build large and substantial barriers between them and the rest of the economy by means the use of loyalty or subordination, exchange of goods and resources, joint use of personnel and management control, shareholding in other companies (including potential or actual competitors) and in general through various types of market and non-market arrangements. Obviously, an analysis focused on these issues, will differ widely from one who sees the companies just as organizations seeking to minimize the transaction costs that they face in the market.

64 For example, an eminent Institutionalist, Professor Ha-Joon Chang, prefers radically differentiate the NIE (associated to Nobel laureates, professors North and Williamson) from what he denominates Institutional Policy Economy (IPE). Another reputed Institutionalist academic, Professor Geoffrey Hodgson (2006), tends to identify his evolutionary perspective with some aspects of the Old Institutional Economy (OIE).

In our analysis, we do not share the point of view of professor Williamson, who put forward a model of individual human nature characterized by opportunism and recklessly. Using his approach assumes the implication that it applies equally to the market and the firm and additionally assumes the institutional environment as granted, giving small recognition to the effects of the institutional environment in moulding actions and beliefs, but only stressing their influence in determining the general constraints to market agent's actions.

In contrary to that approach, we are closer to proposals of other institutional thinkers (e.g. Bowles, 1985, 1986; Hodgson, 2004, 2006)) who do not assume levels of cooperation and trust in a society as endogenous variables related to individual nature, but rather as being mostly a function of the involved institutions and structures which conditions individuals conduct (Gintis, Bowles et al., 2005; Koutonen W. 2004; Koutonen F. 2006; Tomasello and Vaish, 2013; Andreoni et al 2016).

That means that in those non-neoclassical institutional approaches, the nature of the firm is rather related to power than to efficiency, and that focus explained firm performance on the base of their ability to extend the market power of their owners, and not by means of technological progress. This approach contrasts sharply with the version of Coase and Williamson in which the existence of the firm is basically explicated in terms of efficiency and minimization of costs (Williamson 1985:68-84). However, we understand that NIE is an emerging approach, that can be described, using Williamson's words, as "*a boiling cauldron of ideas… (in which) not only there are many institutional research programmes in progress, but there are competing ideas within most of them (and there is a vast amount of unfinished economic-refinements, extensions, new applications, more good ideas, more empirical testing, and more fully formal theory*" (Williamson, 2000).

For a long time, institutional issues have been acknowledged by neoclassic economics as intrinsically linked to the themes of technological change, the coordination of economic actors, the distribution of income and the convergence of growth and productivity (Jorgensen, 2009). In addition, these issues are considered determined by changes in relative's prices.

However, from an evolutionary and institutional perspective it is possible to arise a research topic neglected by the orthodoxy; the question if these new relative prices, rather than affecting the pre-existing institutional structures, are affected by that

institution´s framework and that, for the economically interested actors participating in the process. Also, from this perspective, it is valid question to ask if in this game of mutual determinations, there are relatives prices, or, on the other hand, history and institutions are the ones who ultimately play the central role.

Each one of these areas defines a particular set of rules of the game that determines the income distribution and the overall performance of the economies. However, institutional analysis shows us that not all the institutions are in a condition to define themselves by the performance and income distribution potentially achieved by an economy (Michelbach et al., 2003).

In general, market institutions (e.g. the system of relative prices) are not in a position to exert that role, or at least are not in a position to do that disregarding the historical conditions and social structures in which an economy is immersed.

In this particular case, historical conditions are especially important given that, in the Chilean economy as in every complex economic system, *"Each human being (and the society as a whole), carries the baggage of its past. Evolution builds on past survivals that encumber action in the present. Choices made by our ancestors can be difficult to undo"* (Hodgson; 2001:3). So, understanding the links between past and present appears to be essential for a good understanding of the process that we analyse in this research.

The mainstream analyses of the Chilean economy generally follow the tendency to "forget history", assuming that historical variables have little relevance. However, it is not the same thing to underestimate the influence of historical specificity on economic analysis, as it simply ignores the incidence of historical process in definition of economic issues.

The appropriate model for studying Chilean institutional change must be widely supported by an understanding of specificity of political and historical context in which they arise. In much of the research undertaken with regards to Chile (generally carried out abroad), it is frequently observed that analyses are developed in a sterile way, using the foundations of the neoclassical economic theory, focusing from there on the analysis of empirical elements that may validate some conceptual hypothesis (usually neoliberal) previously selected.

In the national discussions of the same issues, all different analytical perspectives (especially neoliberal) do not offer a historical approach, emphasising from a political perspective the historical contexts from which their research questions emerge and projecting from their political consequences. These, almost without exception, link the analysis developed to the national controversies about the achievements of neoliberal policies applied from 1973 onwards, in relation to realisations of the 1940–1970´s import-substitution policies and the attainments of socialist policies on which Chile embarked between 1970 and 1973.

After almost eighty years (1939–2016) of structuralist, socialist and neoliberal experiences, the main contemporary Chilean discussions are trying to scrutinise the continuity or not of the neoliberal approach as their role as prime driver of the Chilean Model of development. However, national debate continues to be anchored on this distinctive historic element, as it is virtually impossible to analyse any topic with policy implications, without referring to some benchmarks periods: 1939–1970 (substitutive industrialisation), 1970–1973 (transition to socialism), and the period 1973–1989–2009 (application of the neoliberal reforms in their purest or revised form).

Taking that powerful reality in account, the methodology of this research is also historic and clearly differs from those associated with mainstream analysis. So far, this method has tended to study Chilean reforms from a theoretical perspective that has tried to validate or dismiss the model on econometric foundations.

The popularity of that kind of exercise is in some way understandable. Forty years since the beginning of the Chilean neoliberal experiment, under the influence of multilateral financing organisations and given the intellectual support of some major American universities, trade openness and market liberalisation processes have spread throughout the world. This situation has allowed the neoclassical-neoliberal mainstream to suppress the possibility of considering it as simply one methodological option, instead positioning it as the only possible option in the field of economic analysis.

However, in our view, an exercise of this kind, which disregards the non-economic aspects, clouds rather than highlight the problems under analysis, given that the specific historical and political issues linked to the reforms implemented in Chile tend to be undervalued and neglected.

In our opinion, in the Chilean context, the question is not if such problems can be discussed without reference to the experiments that the country has made in the past eighty years in one or another direction. In fact, even the most radical neoliberal thinkers agree with the incorporation of this sort of context. In our opinion, the problem is another one: The Chilean model of development does not correspond, as its supporters maintain, to the explicitness of a set of "technical options" systematised from the perspective of an "objective" economic theory. It has instead been subordinate to an institutional framework, i.e. a set of rules of the game and governance institutions defined, in terms of the interests of certain social group, in a sphere of the "action arena" essentially political.

2.9. Conclusions

In summary, our research approach, independently of the quantitative analysis oriented to falsify the hypothesis neoliberal analysing the actual outcomes of the Chilean model of development, will give emphasis to the historical analysis of institutional building processes. From there we can define in a proper way characteristics and effects of the institutional environment and the singular institutional arrangements that have made possible the continuity of the Chilean development model, beyond the end of the dictatorship. From this institutional point of view, the last determinants of Chilean economic performance will be deployed not only by the institutional blueprint per se, as the underlying economic structure historically and institutionally determined by this, without which such blueprint by itself would not be sustainable.
However, even though the orientation of this research will be clearly evolutionary, our first focus will be placed on the falsification of the neoliberal hypothesis. That process lets us show, area by area, in which measure the effects of relative prices induced by the trade openness have played a key role in the production of the outcomes (positive and negative) of the "Chilean model". In function of that first exercise, we will later assess whether or not, evolutionary approach offer as a whole better possibilities to explain the issues related to failure and success of the neoliberal proposals.

Chapter 3

Structure and Macro-Tendencies of the Chilean Economy

The objective of this chapter is to analyse the relationships between trade openness, market liberalisation, sectorial specialisation, export orientation and the main features of economic growth process of the Chilean economy. Here is supplied a detailed analysis of characteristics and impacts that trade openness and market liberalisation had on it. The first part of this chapter is dedicated to the analysis of growth process and sectorial specialisation emerging from trade openness and market liberalisation and to analysis of the institutional background in which they are framed. In the second part, we develop an analysis of the concentration of GDP exports and employment induced by trade openness and market liberalisation. In the third part, we report the changes to the wage structure resulting from trade openness and the market liberalisation process, in the context of strong productive heterogeneity and high concentration in internal markets. In this chapter, we also develop particularised analysis of the main institutional mechanism which determine the performance of the export sector and the labour markets operation.

3.1. The Sector Specialisation of the Chilean Economy

The Chilean economy in the course of XX century has been sustained by mining and manufacturing, but after 1973 the agricultural and service sector have developed significantly. After trade openness, the manufacturing sector has lost dynamism in particular, losing its share of the GDP and growing at much slower rates than was expected.

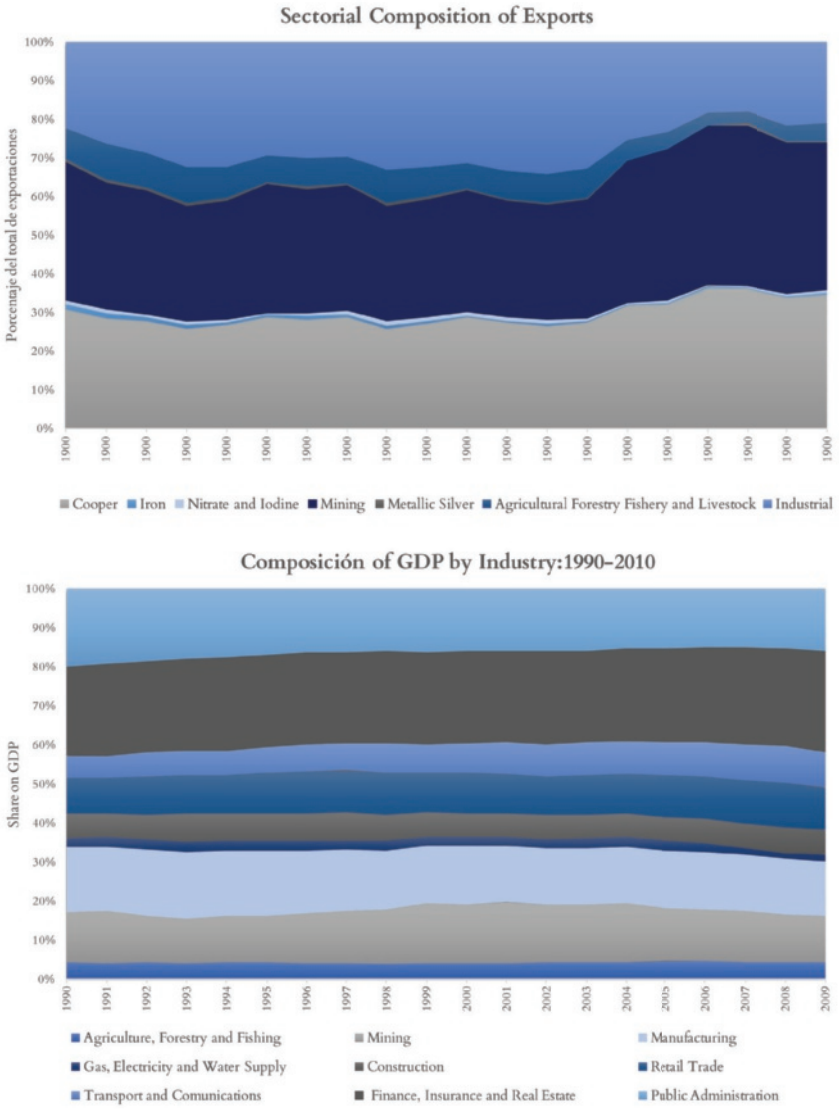

Figure 3.1. The structure of the Chilean Economy
Source: Author's elaboration based on data from the Chile Central Bank (2012).

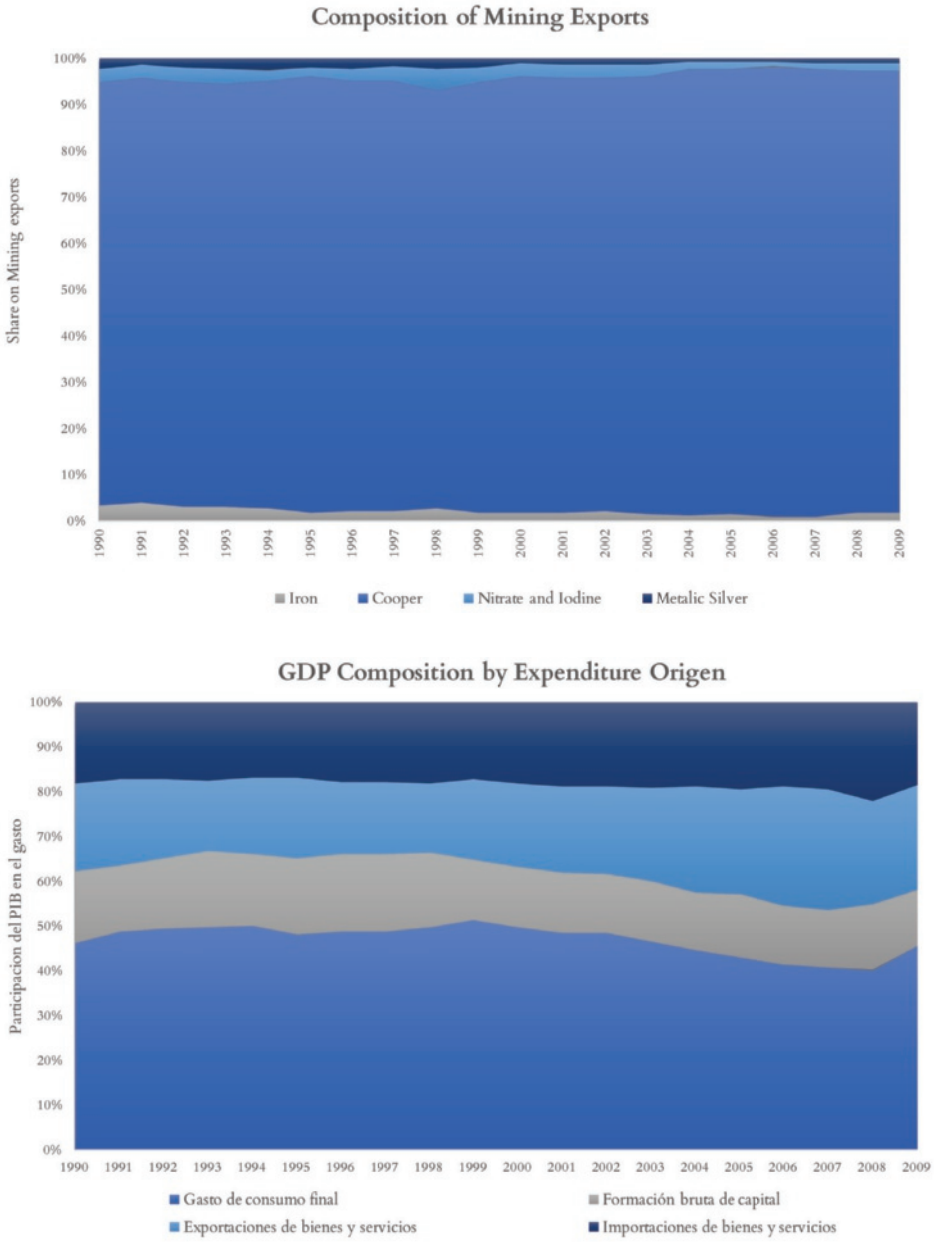

Figure 3.1. Continued.

The structure of the Chilean economy is reflected in the boxes of Figure 3.1. The first one shows the composition of its GDP from the point of view of its sectorial composition and the second one from the expenditure structure.

In these figures, one can observe that the country possesses a GDP structure in which the mining sector and the financial sector are the two most important sectors of GDP generation, followed by the manufacturing sector. In particular, mining shows a greater tendency to increase its participation in domestic product.

In the two lower boxes is observed that even though the bulk of exports are of mining products, mainly copper, despite this, domestic product has expanded vigorously (Figure 3.2) throughout the process of economic opening, even though its growth rate seems to have lost its previous stamina following the Asian financial crisis of 1996–1998.

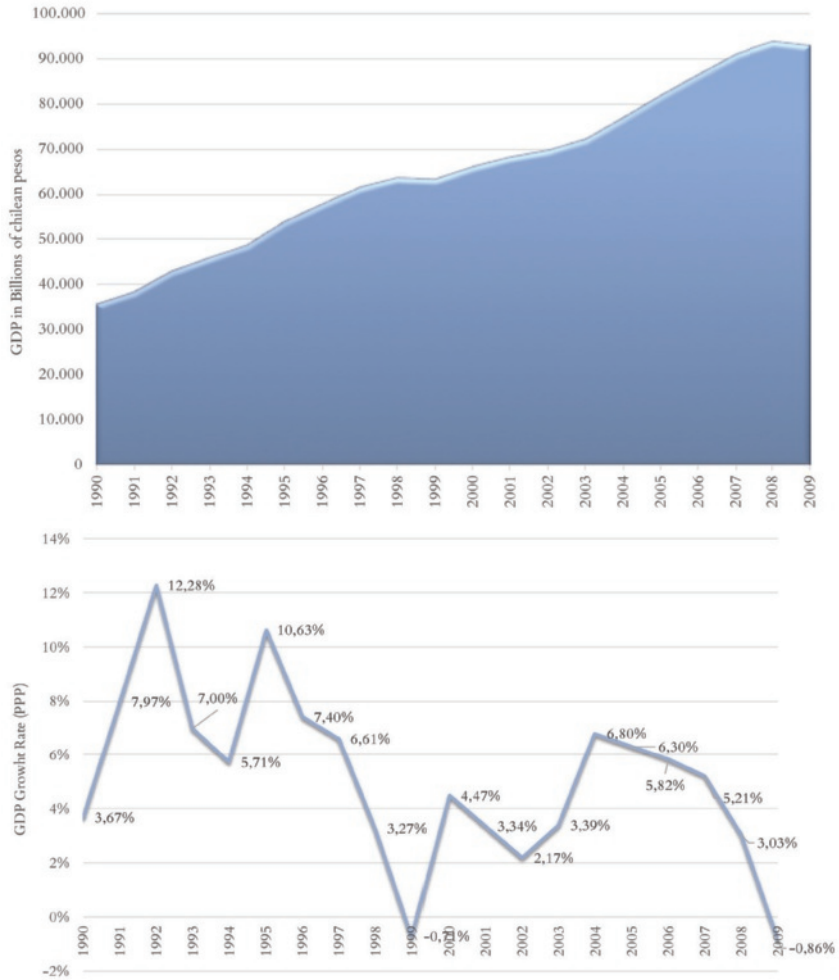

Figure 3.2 Evolution of Real GDP of Chile, 1990–2009
Sources: Chile Central Bank (2012): and IMF (2008).

This mining sector´s concentration has left Chile extremely exposed to the change in the prices of commodities (especially copper) in international markets. Amongst the major issues the country faces is the need to modify its productive structure, which is concentrated not only in terms of the origin of its production, but also in its destination. In fact, during 2009, 95.9% of the exports of the country were linked in some way to its raw materials; 35.5% corresponding to primary products and 54.2% to articles based on these resources (e.g. pellets of iron, refined copper or wine).

This dependence on primary resources is higher in Chile than in other less developed Latin American countries, such as Bolivia and Ecuador. Additionally, Chilean exports are very geographically concentrated. In 2009 49.7% of total Chilean exports were destined for the Asia-Pacific region, particularly China, a share that widely exceeded the Asian export share of other Latin American countries such as Brazil (28.2%), Peru (26.5%) and Argentina (18.2%), (ECLAC, 2012).[65]
As an average of the analysed period, exports constitute 30% of GDP and imports 40%; meanwhile, the internal demand for local production has fallen significantly. A revaluated exchange rate introduced changes in the quantities demanded internally from abroad for domestic consumption or investment. The increase in domestic demand is essentially explained by the increase in the disposable income of households, whose incomes have benefited from the increase in exports and the fall in the price of tradable goods (INE, 1998).

The weight of the external sector is remarkable, given that exports and imports explain more than 40% of GDP, with a significant rise in the export sector. The rest of GDP spending is concentrated in capital formation, which shows a downward trend. However, from the point of view of spending, almost half of this is destined for Final Utilisation (BCCH, 2011a).

The export structure of the Chilean economy includes a high share of the industrial sector, which in 1990 amounted to 33%, reaching a maximum of 48% in 2002, returning then to 33% towards the end of 2009. However, exports incorporate a low proportion of value added, being essentially composed of commodities that are highly intensive in their use of natural resources (cellulose, iron pellets, etc.). Agricultural-forestry and marine products, which in 1990 reached a maximum share of 12% and, in 1991, a share of 14%, have increasingly lost participation in exports, coming to

65 In a complementary way, 18.2% of Chilean exports (2012) went to other Latin American countries, 17.2% to the EU and 9.9% to the USA.

just 7%, in 2009 after slightly exceeding its basic level of 5% recorded during the biennium 2006-2007. Meanwhile the mining sector, which in 1990 accounted for 54% of exports, temporarily decreased its share because of the development of the Asian crisis of 1996-1998, which produced a declining demand for mining products (Corsets et al.; 1999).

Subsequent to this, the mining sector continuously increased its participation in exports, reaching up to 60% in 2009 (op. cit.). Chile is the world's largest copper producer, generating 36% of world exports of this metal. The mining sector was centred on copper production that in 2009 rose to 13% of GDP. Chile's other primary export products include fruit and vegetables, wood and salmon. Within the industrial field, the export of wines is crucial. This sector has acquired great importance and dynamism in the last decades. Industrial production is also focused in areas such as dairy farming, wood and cellulose.

During the last forty years, Chile has failed to reduce its dependence on copper exports. During the 1960s they accounted for 70% and in 2009, Figure 3.1 shows that copper exports were close to 60% of total exports. In general, we can see that during this period Chile has not reached a major level of industrial production with substantial added value.

The reallocation of resources and the re-building of the industrial fabric that was produced by the unilateral opening of the 1970s and 1980s, as well as the Free Trade Agreements (FTA) of the nineties has not resulted in a sustained growth of GDP and productivity in a way proportional to the radical nature of the changes induced after 1990.

The dynamics of the Chilean economy between 1990 and 2009 were characterised by the sustained growth of domestic demand and the stagnation or decline in exports of manufactured goods considered as a whole.[66] Real GDP growth is explained to a great degree by the increase in the terms of trade and by the concentration of exports in commodities of high international prices.

66 At the point in time of the conclusion of this study (2016) this situation has not essentially changed.

3.2. The Bright Side of the Moon: The Times of High GDP Growth

According to the OECD database, in 2009 the value of the Chilean GDP had already reached USD270 billion, a superior level to that exhibited by Ireland that year (USD183 billion). From 1990 to 2009, Chile has practically doubled its size, surpassing Israel whose GDP was only USD207 billion in 2009 and Pakistan with a GDP of almost USD168 billion. However, these figures remain a crucial limitation of the Chilean model of development because of their high dependence on mining and other primary resources and their accentuated process of de-industrialisation (Palma 2013).

Despite this shortcoming, according to estimates from the World Bank (2012), during the 2010-2016 period, Chile is likely to raise from a per capita GDP measured to parity of purchasing power (PPP) of USD16,084 (in 2010), to a per capita GDP (PPP) of USD23,000 (in 2016).[67] In support of these forecasts, in 2009 Chile already had the largest Gross Domestic Product per capita (based on purchasing-power-parity (ppp) in the region) with US $14,299,372, beating Argentina which that year showed only $14,125,568.

The IMF has also estimated that at the end of the year (2015) Chilean GDP per capita PPP will be US $23,556 (IMF, WEO, 2014), approaching nations such as Portugal, whose GDP is expected to be US $27.624. However, obtaining these growth goals will be hard, and it will be harder still to achieve the development targets associated with these growth forecasts.

As we can see from Figure 3.2, the ground rates of the expansion of Chile's GDP have been systematically decreasing. In fact, given that Chile wants to equal Portugal's GDP per capita by 2016, the average GDP per capita (PPP) growth rate of 5.1% that Chile has exhibited during the period 2000-2009 (OECD, 2012) would have to be upgraded to levels closer to 6.0% annually, from 2010 onwards.

Unfortunately, this has not happened; the growth rates of the GDP per capita between 2010 and 2015 have been only 4.2% and from 2016 onwards, the projected rates are lower than 2% annually. Only if the international economic situation does not worsen

67 At the time of concluding this investigation (2017), The World Bank projections have been fully met. In 2013, the OECD reported that Chilean GDP pc (ppp) was US $22,000, and the IMF estimated that Chilean GDP pc (ppp) 2014 was US $23.165,

beyond the expected 2.0% GDP growth forecast by the Chilean authorities,[68] perhaps by the year 2025, Chile will be able to reach the 2015 level of GDP per capita of a developed country such as Portugal. Although this level of GDP would be below expectations, obtaining it would be an important economic achievement that no other Latin American country is in a position to accomplish yet; however, that possibility seems to be remote.[69]

3.3. The Economic Concentration Process

In spite of its export-led growth path, Chile has essentially remained a highly-concentrated economy on which a small, but well-positioned group of large corporations has progressed and taken control, not only of foreign trade but also of significant sectors of internal markets previously occupied by smaller enterprises. They have replaced smaller enterprises not only in their shares of sales and GDP, but also as employment generators, a situation that has radically changed the behaviour of labour markets. Large enterprises, being a small number, concentrate an important proportion of sales. On the contrary, the important number of small firms concentrates a reduced proportion of sales.

3.3.1. Product and Sales Concentration.

Sales are not the same than Gross Value of Production (GVP), but if sales of each size of economic net of taxes are adjusted by their stock variations, we get the GVP of these companies (GVP). When this amount is multiplied by the sectorial technical coefficients of the input output matrix (VA /GVP) we can obtain the real value added (VA) of the economy, i.e. the GDP. Unfortunately, the Chilean national accounts do not permit us to visualise in a direct way, what degree of responsibility each size of enterprise has in the generation of the GDP. Despite this, the country's tax authorities

68 http://www.economiaynegocios.cl/noticias/noticias.asp?id=138867

69 This is not an easy target. Given the effects of the current international recession in Europe and the United States (two of the three main markets for Chilean exports), Chilean growth rates were, between 2010 and 2012, equal to 5.75%. They are expected to be more modest in the next period (2013-2016), moving around the low annual 5% in the best-case scenario. Chile's economy is entering a mild slowdown phase after years of strong growth. The Government of Chile expects a GDP of tendency of less than 4% (the original figure was 5.5%). The figures were determined by the "GDP Trend Committee", a body of experts convened by the Chilean Ministry of Finances.

have delivered from 1990 onwards extremely detailed statistics of sales produced for each size of firm.

According to the figures already exposed and to those we will present in Figure 3.3, it is clear that the path of evolution of the GDP is very similar to the aggregation of the sales evolution of firms. However, given the deep productive heterogeneity of the Chilean economy, every size of company has different ratios of VA/VBP and different proportions of stock variations. In other words, every company size generates different levels of value added and contribution to GDP.

Within the Chilean economy there are strata and sectors of very high and very low productivity. As the Central Bank of Chile does not provide technical coefficients of the input-output matrix disaggregated by size, it is not possible to obtain an accurate appraisal of Chilean GDP disaggregated by sizes of enterprises. Nevertheless, as we have already explained, the distribution of sales is a good proxy for its estimation.[70] This exercise will be done assuming that, if we can identify a strong concentration of sales in large companies, the GDP concentration in these companies will be even bigger. So that, using sales information we will identify the trend towards the concentration in which we are interested, regardless of the definition of its exact amount.

70 Aggregate concentration is conventionally measured as the share of an economic variable such as value added, or assets held by the largest firms in a sector or the economy as a whole (Weiss, 1983). Given that in Chile, only data covering the total sales of companies of all sizes is available, and value-added figure numbers are not obtainable, we will use sales share as a proxy variable of the concentration.

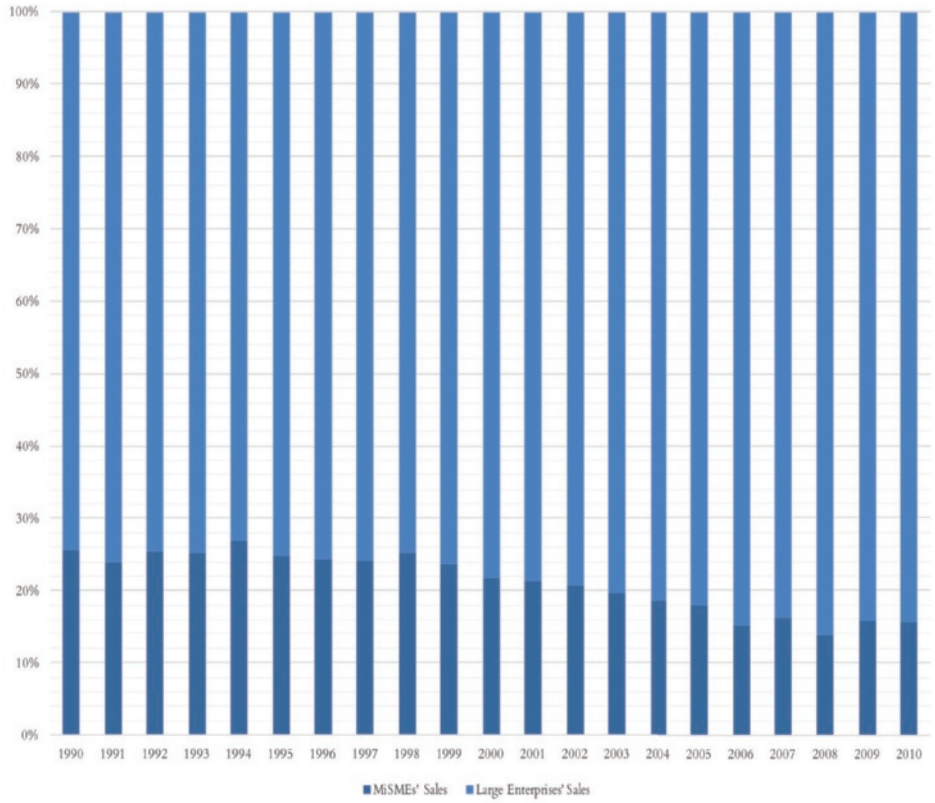

Figure 3.3. Sales by Size of Firms, Chile 1990–2009
Source: Author´s elaboration using data from the Chilean Internal Revenue Service (1990–2009).

This situation shows Chile to be an economy, vis à vis its trade openness and market liberalisation, which is increasingly heterogeneous and with a growing separation between the market share of the large-scale modern sector and the market share of medium, small and micro enterprises. Figure 3.3 shows that in 1990 sales of Chilean large-scale firms were 2.9 times the sales of MSME; twenty years later, in 2009, LSEs sales were 5.3 times sales of MSME (ibid).

Obviously, this displacement of sales and production from one scale to another is a manifestation of a major process of resource reallocation between sizes of firms, involving not only physical investment but also processes of labour mobility from the backward sectors to the more productive ones.

The Chilean economy is divided into two loosely connected worlds, one of high and another of low productivity, among which both labour force and capital, should be

reallocated.[71] However, if the positive factor´s reallocation is not actually detected, a sound hypothesis that may explain that result could be the consolidation of a framework of high structural heterogeneity over the economy as a whole. That situation would mean that there are large productivity and production differences between different sectors and size of firms.[72] If we review the evidence that must give support to that hypothesis, there would be at least two facts that seem to be sufficiently clear, given the empirically available evidence:

1. The average productivity of Chilean MSMEs is significantly less than large enterprises' productivity (Infante, 2011).
2. As a result of their low and declining productivity, the bulk of Chilean MSME are not in a condition to face competition in an adequate way (Pagés, 2010). This means that, following the openness of the economy, they have neither been able to face competition arising from foreign products (mainly Asian) nor internal competition coming from big business groups that dominate the Chilean economy.[73]

71 The "first world" (Large Scale Enterprises) drive the economy and pay better wages (but not as good as would be expected), while the "second world" (MSME) have little impact on growth, notwithstanding that they create much of employment (INE, 1993, 2013). This dual structure does not correspond to that modelled by Lewis (1954) in trying to reflect the path of development that should occur in the backward economies. Rather, it reflects, as Acemoglu and Robinson argue (2012:258-271), a specific and deliberate way of constructing an extractive economic model.

72 Such phenomena were originally described under the name: "structural heterogeneity (SH) of peripheral economies". This is a complex concept that begs more than one definition. Some authors, like Nohlen and Sturm (1982), report at least eleven different meanings. Nevertheless, on its historical matrix, SH was viewed as the presence of activities and/or production branches in which the Average Productivity of Labour is similar to that of central economies, but coexists with backward technological activities in which productivity levels are significantly low. The first generates jobs and incomes and the latter absorbs underemployment (Pinto, 1959, 1970). The presence of high levels of SH is an essential difference between developing and central economies. One of the most recent analysis of the heterogeneous behaviour of Latin American economies can be found in Infante, 2011.

73 It would be interesting to determine in which proportion MSME' declining competitiveness is based on their inability to face imported substitutes, or is the result of competition arising from large companies that operate within Chilean domestic markets. However, independently of this measurement, the disarticulation of the productive fabric and the generation of a competitive gap between MSME and large enterprises is beyond any doubt.

After 1990, according to the official Chilean statements, the presence of productive heterogeneity would be seen as a feature of underdevelopment that should be overcome, given the orientation of new public policies of development (Foxley, 1983:45-52).

However, as we will analyse in chapters IV and V, rather than the expected convergence of Chile with the linked and diversified economic structures of the central countries which Chile sought to emulate (ECLAC, 1998, caps. III and IV), a process of growing heterogeneity, concentration and weakening of market competition, like the described in comparable contexts by Armstrong and Sappington (2006), is clearly observable.

The fact is that in Chile; about 98.5% of the economic fabric is constituted by MSME of extremely reduced scale (SII, 1990-2009). These firms suffer severe productivity limitations and low access to production factors, elements that are a significant limit to the evolution of the economy, especially given that this situation has worsened during the process of trade openness and liberalisation (Román, 2000; Bianchi y Davide 2002; Cimoli y Kast 2003).

In addition, as Figures 3.4 and 3.5 shows, there is a serious break between a modern and relatively efficient sector (LSE) and a slow and backward sector represented by MSME.

At first glance, Figure 3.4 seems to contradict that assessment and express a certain consolidation of the productive fabric formed by MSMEs, which (with the exception of microenterprises operating at the borders of informality) are numerically growing, a remarkable phenomenon in any economy.

Figure 3.4. Evolution of Share of Number of Firms by Size
Source: Author´s elaboration using microdata of SII Chile: 1990-2010.

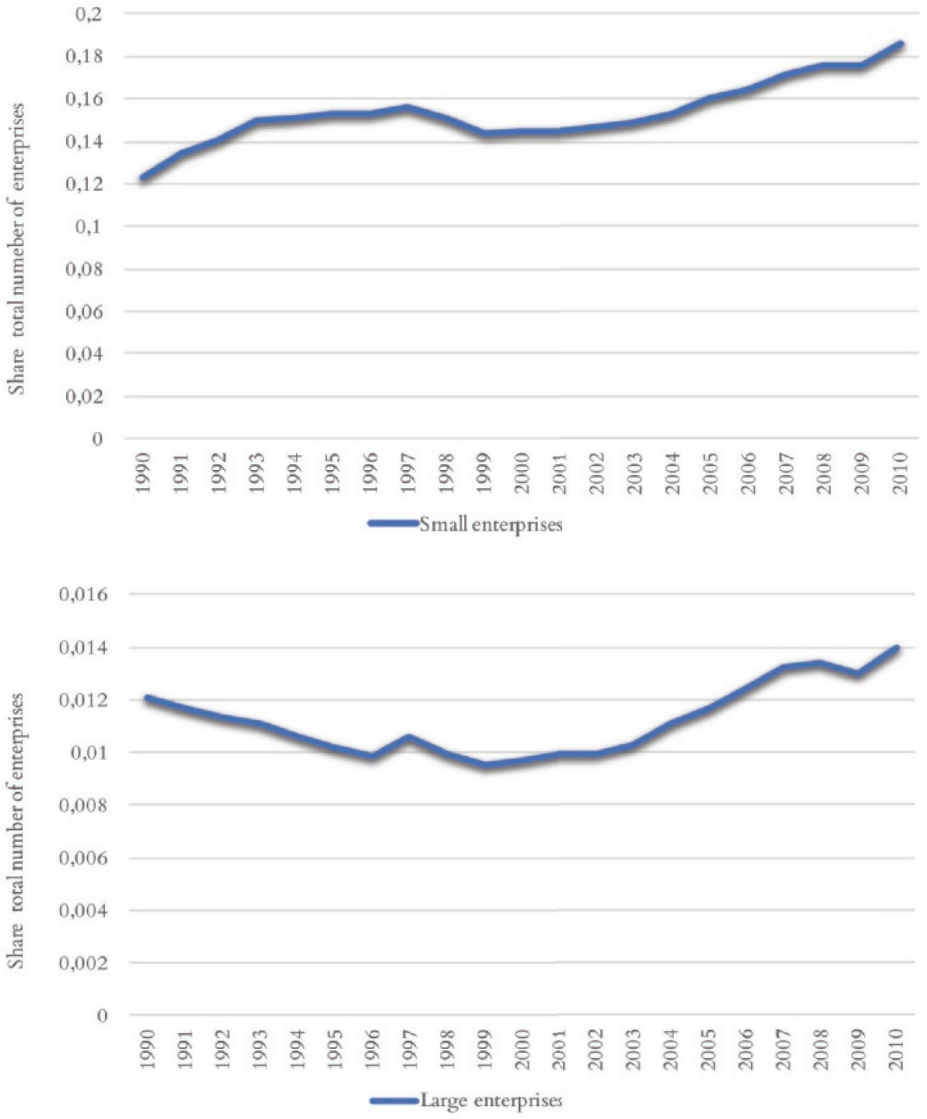

Figure 3.4. Continued.

Given this situation and the progressive nature of official discourse, it would be reasonable to predict that Chilean public policies would translate the enlargement of markets into a context of higher economic opportunities for all sizes of firms.

This would then be expressed in the presence of a growing number of MSME trying to utilize that new opportunities, associating the arising higher number of firms with

abstention of a higher market share for these ones. Nevertheless, this has not occurred to date. In fact, in Figure 3.5, which shows the sales distribution from 1990 to 2009 disaggregated by company size, we can observe a clear tendency that contradicts this expected outcome. Along trade openness, whilst the numerical participation of large corporations maintains a proportion fluctuating among 1.2% and 1.4% of total number of firms, their sales' share increases from 74% to 84% in twenty years. At the same time the share of MSME diminished from 26% to 16%. Within MSME, the micro enterprises share dropped from 5.5% to 2.2%, the small companies share dropped from 14.1% to 6.9% and the medium firms' share dropped from 7.1% to 6.8%. (SII, 1990–2009). If the value of the new sales share of large companies is compared to their old sales share value in 1990, we see (over the twenty years under analysis) an important reduction in absolute value of market share of MSME. For that reason, Figures 3.4 and 3.5 show that Chile has been producing one of the greatest dynamics of economic concentration ever recorded in its history, transferring a large amount of economic resources not only from labour to capital, but also from smaller enterprises to the largest corporations.[74]

74 As a result of such concentration, according to the information recorded in the UCSF (Uniform Codified Statistical File; FECU in Spanish), which is the instrument through which Chilean corporations report to the Superintendence of Values and Insurances, the sales of the ten largest companies alone in the country are equivalent to 38% of the Chilean GDP (FECUS 2007). Likewise, in 1999 three business groups concentrated 74% of the capital of all companies listed in the stock market, and ten business groups 89% of this capital (Agosín and Pastén, 2003).

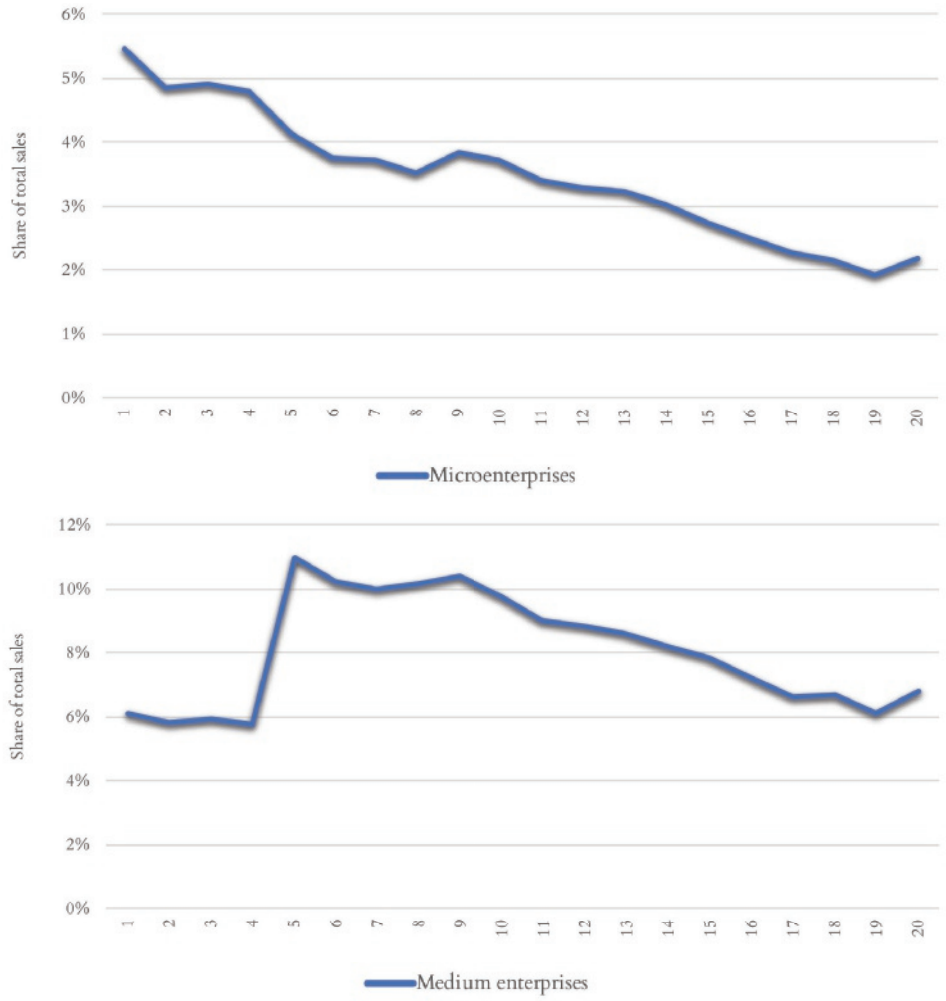

Figure 3.5. Evolution of Participation on Total Sales by Firm Size. Chile, 1999-2009
Source: Author´s elaboration using microdata of SII Chile: 1990-2010. Sale´s values are exprese4d in UFs.

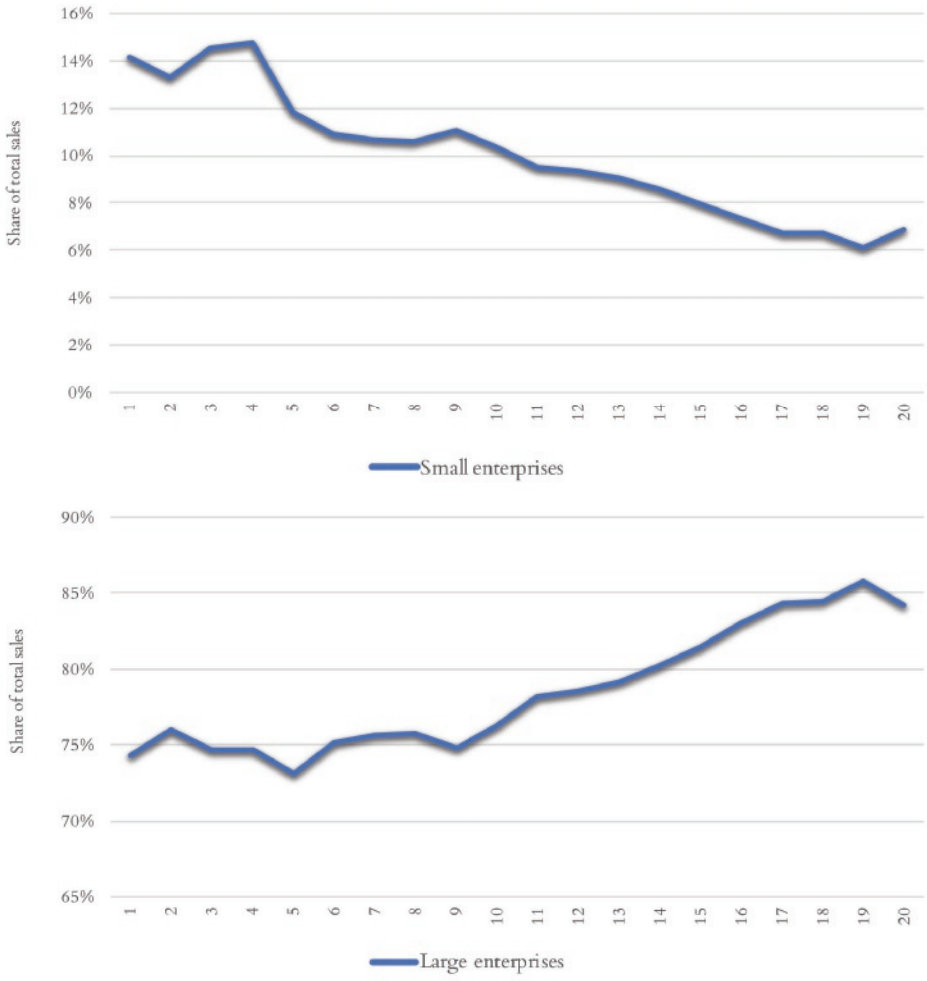

Figure 3.5. Continued.

This sharp deterioration of the position of the MSME, which happened in a way parallel to the trade liberalisation, may be attributed to multiple causes. Some authors, as Ruben, et al. (2006) affirm: *"analytical approaches for addressing the role of trade for development involve a mixture of disciplines that focus on issues of efficiency, organization and innovation as key dimensions of competitiveness. Smallholders participation in global supply chains is critically determined by three processes: market access, network governance and chain upgrading".* Based on this approach, we will test the possibility of widening this hypothesis beyond the supply chains area.

In next chapters, we will examine if this approach could be applicable to the analysis of the Chilean economy as a whole, including all backward and forward linkages that characterise the various sectors of the economy, and not just to certain supply chains where the phenomenon described above exists as an unquestionable fact.[75]

3.3.2. Institutional Arrangements and Lack of Competition.

Given that MSME situation is clearly determined by the first two variables, market access and network governance. The third (chain-upgrading) is greatly similar to the process of dissemination of technological progress and exert a less direct influence. In any case, the Chilean case these three variables as a whole, seem to be the factor that explains declining of small size enterprises' sector.

Given the raising weight of the LSE as originators of GDP, from the neoliberal point of view was assumes that resources reallocation process would have produced an improvement in the growth rates of the economy because the trade openness has implemented a major process on the resources reallocation from MSME to LSE. Given this assumption, when it was necessary to implement specific policies during the Asian Crisis, policymakers hardly influenced by that perspective, protected LSE from its negative effects because they characterised (ex-ante) these segment of firms as a repository of the better quality productive factors and better technologies.

It was obvious that the Chilean Governments (1990-2009) did not consider that the sector of large enterprises should be restructured in base to external competition. They

75 Our opinion is based on the results of the observable linkages existing in the Chilean economy between sizes of companies. This issue will be addressed in the chapter VI in which we will test this hypothesis through the breakdown by size of the last input output matrix available in the country (2008) which practically coincides with the end of the period under analysis.

were intending only restructure the MSME sector that was in a vulnerable situation due to rising short-term interest rates[76] and with no delay, all policy measures of the Chilean government were adapted to this view.
Because of that decision, between 1990 and 2009, the escalation of the real value of LSE´ sales share during that period was quite significant. From figures on Table 3.1, is clear from the fact that small companies have been rapidly losing the market shares which they traditionally operated. That is not a situation present only in certain productive chains, but it has reached a universal character.

The strength of this outcome is expressed in the available aggregate figures that represent the behaviour of markets. The general loss of participation does not obey only to events what happens in the major sectors and value chains in which the Chilean economy specializes. On the contrary, as we shown in the Appendix I in which sales figures are reported disaggregated by sector, it is a phenomenon which commits to all economic sectors and practically all their supply chains.

The smaller and declining share of the MSME in the sales of each sector and on the economy as a whole, is empirically due to combination of two phenomena:

1. The first is the expulsion of firms from different markets, produced by institutional arrangements that leave them out of play in the processes of competition in markets in which they are traditionally involved, closing your subsequent access to them.
2. The second is the creation of impediments to new firms that want access to these markets. These barriers are generally derived of specific institutional arrangements that strengthen the position of dominant larger firms, closing the doors to the inclusion of those companies that defy such dominance.

76 When in 1998 the Chilean authorities decided that it was necessary to curb aggregate spending in the economy in order to address the external constraint produced by the Asian crisis, they had only two tools to hand: the nominal exchange rate and the short-term interest rate. When they chose the latter as the adjustment variable, they severely hit MSMEs indebted to floating rates. However, they isolated from many of the effects of the crisis to the large companies that generate the GDP and that, in order to finance its expansion to other countries in Latin America, were highly indebted in dollars at fixed rates. Supported in these measures, government expenditure and the expenditure of large companies remained constant and had access to external long-term financing. On the other hand, MSMEs were isolated from the positive impact of this policy instrument, insofar as short-term borrowers were those who suffered the biggest impact of rise in short term interest rates, variable that was used in order to contain spending of Chilean economy.

Table 3.1. Real Value of Chilean Firms 'Sales: MSME and LSE 1990-2009

YEAR	Micro Enterprises	Small Enterprises	Medium Enterprises	MSME	LSE	Total Sales
1990	145	375	161	681	1.975	2.656
1991	155	426	186	767	2.430	3.197
1992	168	498	202	868	2.559	3.427
1993	178	551	214	943	2.785	3.728
1994	200	577	533	1.310	3.558	4.868
1995	210	613	571	1.394	4.216	5.610
1996	224	642	600	1.466	4.554	6.020
1997	220	664	639	1.523	4.763	6.286
1998	242	696	653	1.590	4.705	6.295
1999	240	669	630	1.539	4.935	6.475
2000	245	683	645	1.573	5.623	7.196
2001	248	704	666	1.617	5.933	7.550
2002	257	723	684	1.664	6.330	7.995
2003	268	763	726	1.756	7.138	8.894
2004	268	781	768	1.817	7.980	9.796
2005	272	819	821	1.911	8.786	10.697
2006	280	866	863	2.009	11.293	13.302
2007	277	895	901	2.073	10.754	12.827
2008	279	922	938	2.139	13.348	15.487
2009	313	992	975	2.281	12.149	14.430
TOTAL SALES	4.688	13.858	12.375	30.921	125.816	156.737

Source: Author´s elaboration using data of SII Chile: 1990-2010. Real values of sales are expressed in millions of UF.

Within the institutional arrangements that cause both the exclusion of companies previously incorporated into the markets, as the access of those companies that have not yet joined them, include two elements of great importance:

i. Arrangements that allow unilateral changes in the interest rates applied by banks in the short term, which are those that define profitability of the MSME projects, inducing them to access only to short-term and high cost loans.

ii. Arrangements that define the scale of public and private biddings used by both sectors to buy its inputs (goods and services). In this way MSME are required of large amounts of working capital and ballots of bank guarantees, elements which frequently are not available to small firms due to lack of collaterals. As a result of that, MSME are unable to access to greater part of these markets.

Arrangements of this nature and others which we will discuss later, affect as it is raised by O.E. Williamson (1996:330-332)[vi] the three main areas of governance of markets: Investment; Contracting and Discriminating Alignments.

In the area of investment, it is clear that the two large institutional arrangements mentioned above, define the decisions between debt and equity to be taken for each size of firm and also define the administrative costs of paying compensation and disincentives for future investment of each one of them. Depending on the characteristics of each firm's the nature of its assets also plays a relevant role in the presence of "demoralization costs" (Michelman, 1967) and on the farsighted approach to investment and "security expectations". However, in our opinion, from the perspective of the small-scale firms, all these factors are not concomitant to an eventual malevolence of the State, but rather of the actions of larger business groups. In such a way, the stability of the rules of the game at every level, as well as the particular market´s arrangements that weaken the ownership of its assets are linked, in the view of MSME, to the greedy actions of the business groups, more than to the "State deliberate actions".

Available studies on the evolution of the business turnover, disaggregated by size of companies, confirm our appreciation, reporting that those sectors that have greater economies of scale and market power, tend to have a lower rate of entry (Benavente y Külzer; 2008). An increased level of difficulty of new companies 'access to the markets, as well as the removal of MSME from these, has been accelerated by the institutional arrangements described above. Them has been defined and vertically enforced from the LSE that dominate different markets while the Chilean State has played (before and after 1990) a role of collaboration with this process. The state has established legal and administrative frameworks that leave extremely confined the spaces from there would be possible to establish modifications in institutional arrangements, otherwise replaced them by others more favourable to the non-dominant companies.

That combination of private public interventions has established and consolidated a model of networks governance which has been extended to sector-to-sector, becoming a

national model of marked neoliberal inspiration, which, with small sectorial specificities, has been imposed at the aggregate level. It is precisely the specificity of this model of governance that has been installed in the industrial fabric Chilean, become the origin of the vertical LSE´s control of the markets and of the great market power who them has being accumulating.

As we will establish in the next chapters, all that has produced serious difficulties in the dissemination of technological progress and also has induced severe difficulties, sector-to-sector, in the field of chain upgrading. The absence of the concerned upgrading has been transferred from chains to sectors and from there, to the economy as a whole, being its most conspicuous expression the stagnation and fall of multifactor productivity in the Chilean economy, another issue that also will be subsequently analysed.

3.4. The unexpected Outcome of Trade Openness

The neoclassical and neoliberal analysis of the Chilean economy generally argues that, because of reforms post 1973, the country would embark on a path of robust growth and specialisation in areas of increasing aggregation of value and clear export orientation. However, these theories must confront the fact that Chile remains heavily dependent on the exportation of raw materials, mainly mining products. Trade openness, far from limiting such orientation, has exacerbated it. In spite of the increasing primary specialisation of the Chilean economy, it did not seem to generate too much concern in any of the wings that the 'model advocate' economists were grouped, i.e. the orthodox neoliberals and the supporters of the NEGT.

The roots of the Chilean policies that allowed this process to occur can be traced to the intellectual influence in the Chile´s political and academic life, of a renowned group of academics of MIT and Harvard University who have been at the forefront of the NEGT and Endogenous Growth Theories. (Aghion and Howitt, 1992; Robinson, 1998; Aghion and Durlauf, 2005; Aghion, Fedderke et al, 2008, Acemoglu, 2009; Acemoglu and Robinson, 2012). They commonly refer to their paradigm as "Neo-Schumpeterian Growth Theory" and, positing the mechanics of innovation-generation as a central issue, they promote process of "creative destruction" that looks similar to those formulated by Schumpeter (1942).[77]

77 Schumpeter´s definition includes a "*process of opening up of new markets, foreign or domestic, and the organizational development from the craft shop and factory to such concerns [...] that incessantly revolutionizes*

The core of this view of economic development is fairly simple. Economies progress insofar as they are not exclusive and become inclusive. Inclusive economies are being built, in the majority of cases, by political and economic institutions of inclusive character. Meanwhile, when the prevailing political institutions and the new ones are mutually exclusive, if the incumbent institutions prevail, power will not be distributed broadly, will tend to enforce economic institutions that expropriate the resources of the many erect entry barriers, and suppress the functioning of markets so that only, a few benefits (Acemoglu and Robinson 2012:81) and the economies will develop an extractive character. This means that its objective will be to extract revenues and wealth from one sector of society to benefit another.

The key to differentiating one option from another (exclusive from inclusive) is ultimately whether institutions are deploying process of installation of new innovative, competitive and synergistic economic activities, with the new inclusive institutions that struggle to consolidate. On the other hand, the decline and substitution of the old and unproductive economic activities, in which extractive institutions are supported tend to be associated to the concept "creative destruction".[78]

Schumpeter described creative destruction as a "…*process of industrial mutation…that incessantly revolutionizes the economic structure from within, incessantly destroying the old one, and incessantly creating a new one*." (Schumpeter 1975: p. 83). However, we are not in a situation in which could be possible to asses that the changes in market share of firms (of any size) are produced when incumbent firms, due to their weak know-hows and skills, succumb, being made obsolete by the radical innovations developed by challenging firms.

In the Chilean case market share changes occur when challenging firms are defeated by incumbent's because these large actors are being supported by a mix of political

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the economic structure from within, incessantly destroying the old one, incessantly creating a new one. This process of Creative Destruction is the essential fact about capitalism. It is what capitalism consists in and what every capitalist concern has got to live in, (Schumpeter op. cit., pp. 82–83.). In a different way than the original version, it stipulated that in developed countries a process of creative destruction is necessary to promote from the state productivity improvements, expelling from market inefficient companies and widening the space to the most efficient companies (Caballero and Hammour, 2000).

78 This point of view has been repeatedly supported by Professor James A. Robinson, at the conference held in Santiago, Chile (May, 2018) invited by the authorities of the new right-wing Chilean government (2018–2022).

extractive institutions, asymmetric rules of the economic game and macroeconomic policies implemented from the State. All these factors seem to be placed within a dynamic which can be associated with forms of the so called "crony capitalism" (Acemoglu and Robinson 2012) and not with process of "creative destruction".

However, within the Chilean economic mainstream (neoclassical and neoliberal) be current the idea that technological progress should be associated – in some way – with the disappearance of the backward peasant economies and the great mass of MSME from low productivity. Dominance of this point of view arises from the period of greater acceptance of neoliberal economic proposals on the part of the post dictatorship authorities (at least from 1998 onwards).

When the Chilean economy faced a large external shock because of the Asian crisis, both governmental authorities and the leaders of the Chilean business groups, used that perspective as a manner of facing this crisis. They implemented cost containment policies associated with the short-term interest rate and the Macroeconomic policies implemented by the State which affected exclusively the MSME (rural and urban). Paradoxically this process was called for them: "creative destruction".

That wrong denomination was widely adopted in Chile. Subsequently, a group of Chilean Harvard and MIT graduates, acting now as public officers,[79] play an important role in defining an action programme in order to support the deployment of public policies tending to enhance that kind of "creative destruction"[80] of "inefficient companies".

Their goal was to displace these firms (generally MSMEs) and replace them by more productive firms (LSE), thereby increasing the aggregate productivity of Chilean

79 Strictly speaking, those policies were implemented by a group of economists under the leadership of the Minister of Finances, E. Aninat (a MIT PhD) and C. Massad (a senior Chicago PhD) chairperson of Central Bank (Both members of the Christian Democratic Party). A deeper analysis of the importance of technocrats in the Chilean political system, especially those trained in Bostonian and other Ivy League Universities, can be found in Silva (2010).

80 The Chilean case exemplified in a sharp way the limitations of the neoclassical approach to economic problems. When Schumpeter spoke about "creative destruction", he was not thinking of short-term public policies, but rather he was trying to identify historical trends in capitalist development. However, at least in the Chilean case, the NGT reading of Schumpeter's formulation is focused on the replacement of the most inefficient companies by others of better quality, a process that they think must be promoted by the State.

economy as a whole. The empirical outcomes of this policy were the expansion of the economic concentration and a growing collusion between business groups. This led to the installation of a wide range of "non-market activities" exerted by larger economic business groups aimed to co-opt the new techno-political elites; strategy that initially was highly successful in attracting non-neoliberal economists and subsequently to the political leadership of the centre-left wing.

3.4.1. Wrong Specialisation and Incomplete Globalisation.

At the root of this distortion of the original concept of "creative destruction", some issues have not been sufficiently explored.

Firstly, the participation of the Chilean economy in the process of globalisation does not necessarily mean that the Chilean economic structure as a whole has been globalised, nor does it mean the country's participation in the global economy has been achieved in a more sustainable way than during the period of import substitution (see Figure 3.6).

Secondly, the presence of this phenomenon cannot be linked to an insufficient "openness"; on the contrary, are the effects of the full opening, which as a paradox, seem to produce this "incomplete globalisation". In fact, even though Chile is considered the Latin American country with the most open economy and with more free trade agreements, towards the end of the period under analysis (1990-2009) and after thirty-three years of trade openness, almost 99% of its 798,073 active formal enterprises did not export. (see: Figure 3.6)

Our empirical analysis of the Chilean economy shows that the theorized efficiency to be induced by the free and open markets, which would have been theoretically consolidated during the setting up of neoliberal policies, have not be relevant to the group of large firms which explain the bulk of Chilean GDP.

On the other hand, MSME that explain around 14% of GDP, participate in export´s activities only marginally (around 1.5% of Chilean export´s value) being subject to strong external competition from imported substitutes of their products, are hence clearly more shaken by the openness.

Unfortunately, such influence has not implied a better performance of them, on the contrary, it has implied their exclusion from the markets, but even whether, at an

aggregate level, the openness would be positive for them (a non-probed assessment), and the final effect would be of lesser significance, given their low GDP participation.

However, the key issue is which, the bulk of the large Chilean companies are not part of global processes of innovation and competitive development. These companies operate mainly in protected domestic markets and not subject to higher levels of competition from global economy. The unique markets challenge faced by these large incumbent companies comes from the fragile MSME.

Raising the banner of "creative destruction" in the middle of the Asian crisis was a great help to larger business groups in trying to eliminate this undesirable competition. The adoption of such policies, far from helping the globalisation and modernisation of the Chilean economy, operated against those objectives and only strengthened oligopoly powers.

After trade openness, neoliberal politician and scholars assumed that the Chilean economy would cease specialising in mining production and the large enterprises in all sectors start to be oriented to foreign markets. However, the Chilean economy remained specialised in mining production and 75% of large enterprises continued oriented to the domestic market in which they were not subject to greater internal export either (NCS-DNA, 2010).
Additionally, the weak compromise of LSE with export activities was complemented by the reduction in the number of small exporters, especially those that exported in an intermittent way.[81]

81 An important element of this tendency is essentially explained by the reduction in the number of small exporters, especially those that export in an intermittent way According to the DIRECON (op. Cit.), 88% of the companies that ceased exporting in 2009 because of the international recession were small exporters.

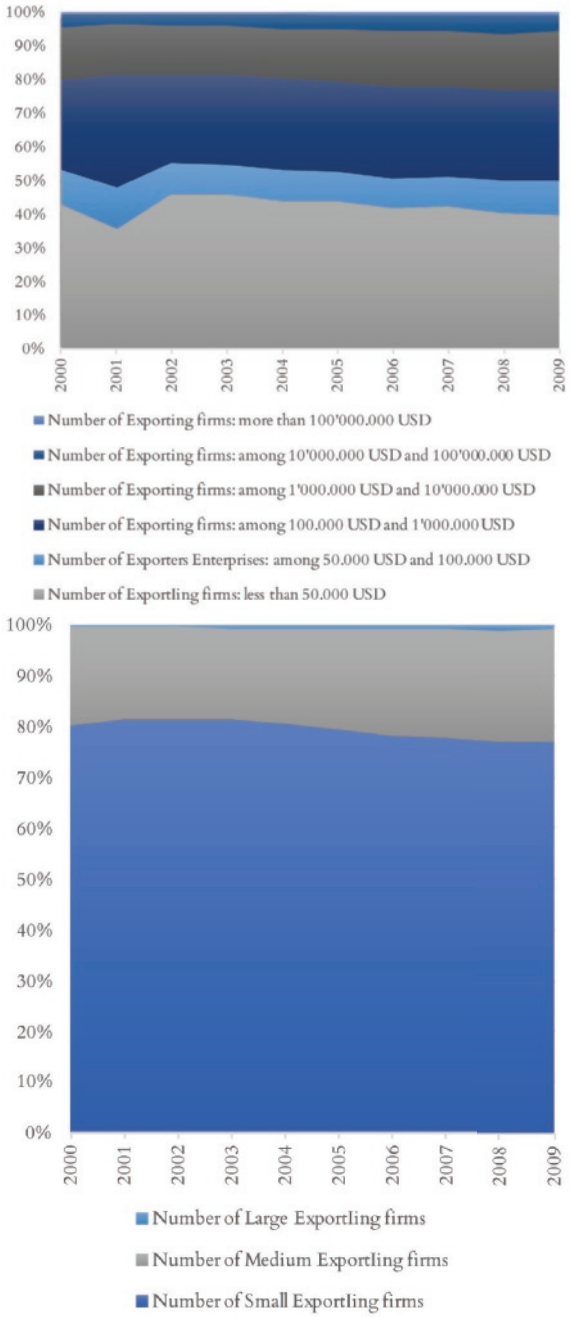

Figure 3.6. Evolution of Participation on Total Exports by size of firms and value of exports. Chile 2000-2009.[82]
Source: Author´s elaboration using data of SNA Chile: 2000-2009 and Direcon 2010.

82 Before year 2000, there are not available information about exports disaggregated by size of firms.

In the last years of our period of study, because of high copper prices, the trend towards hyper specialisation was accentuated, so that mining exports as a percentage of GDP was growing at higher rates than total exports (NCS-DNA, 2012). The intra-sectorial concentration level of Chilean exports is particularly high. For instance, in 2009, 4.5% of Chilean mining companies sent shipments abroad whose value was very close to 100% of the total mining GDP. In turn, the 4.2% of industrial companies exported the equivalent in value of 74% of the industrial GDP, while the 0.9% of agricultural and trade companies produced shipments equivalent to 67% and 45% of the respective sectorial GDP (NCS-DNA, 2010).

In Chile, in a way similar to that reported by Montobbio and Prampa (2005) when they analysed the export performance of nine developing countries,[83] the extreme concentration of the foreign trade sector revealed the existence of serious problems in the dissemination of globalisation impacts on the Chilean economic fabric. If one assumes that exports express the competitive capacity of enterprises, placing products and services in international markets, it would be possible to assess which of these scenarios has not translated into a flourishing number of exporting enterprises, contradicting neoclassical assumptions, and variables that indicate that the competitive capacity of all size of firms of Chilean economy would be strengthened after they incorporation to global markets.[84]

In analysing the Chilean situation, several authors have emphasised the importance of making further progress in diversifying the export basket towards products with greater value added. This is in stark contrast to a current model with a high percentage of exports concentrated in primary goods. This situation means the economy, as a whole, remains very vulnerable to intense and erratic price fluctuations in raw materials (Kharas, Leipzinger et al., 2008; Ffrench-Davis 2010, 2012; Porter, 2011a).

Dependence on those primary commodities, it has been argued, might be a negative factor for the future of the Chilean economy or anyone else's (World Bank, 1993; Sachs et al., 1999; Greenwood and Ananth, 2005). Conversely, it has been argued that, in similar contexts, if export diversification is raised in the short-term, it might "drag" the capacity that the export sector exerts on the rest of the economy. This would be

83 The nine countries are: Argentina, Brazil, China, Colombia, India, Malaysia, Mexico, Singapore and Thailand

84 According to official figures, 62% of the total exporting companies are MSME, but they provide just 1.5% of the value of shipments. This amounts to about 17% of the labour force employed in export companies, employees that earn wage levels not so different to wages paid by smaller and micro exporting companies (Direcon, 2010).

produced by the presence of high elasticity between export growth and the rest of GDP (Aghion et al., 2005, Aghion and Griffith, 2007; Aghion and P. Howitt, 2009).

There are many arguments that support export diversification as good practice. One of these arguments establishes that goods and services with a lower degree of value added are detrimental to the diversification process. This generates complacency in the process and explains the predominance of products involving intensive use of natural resources (Lindert and Williamson, 1985; Lee et al., 2004; Gallego y Loayza, 2005). In answer to these criticisms, some authors (Yeats, 1991; Diaz and Ramos, 1998; Ramos, 1999 and 2001) have emphasised that given its natural advantages, Chile must develop dynamic competitive advantages based on natural resources (forest products, wine, salmon and fresh fruit). According to their views, the success of the Chilean economy must be based on some kind of "Nordic development strategy", based on the growing incorporation of value added to natural resources destined for export. Unfortunately, these ambitions are far from being achieved. Not only has this course not been adopted, but neither has the scope and depth in which the incorporation of value added to natural resources been advanced.

3.4.2. Full Openness with Few Exporting Firms.

According to data from the Chilean Internal Revenue Service (in Spanish SII), in 1990 there were 426,341 active companies in the country. Within that number, exporters (firms and individuals) constitute a least number (4102 firms). Despite this, economic importance of exporting companies is so far to be irrelevant, conforming 41% of GDP and 21% of domestic employment (Direcon, 2010).

Following on from this year, in 1991, 5349 exporting companies accounted for only 0.87% of the total number of operative companies, nineteen years later, in 2009, the direct exporters firms (7519 6502)[85] represented 0.83% of the 782,903 formal companies in operation, displaying a quite small and downgraded exporters' participation on the total number of companies in operation at the country.[86]

85 If, from the 7517 exporters, we exclude individuals and micro formal business and those who export as naturalised persons, the number of exporting firms in Chile for the year 2009 would only be 6,510 (NCS-DNA 2012).

86 In Chile, according to official figures (DIRECON 2008), for every company that is exporting, another five companies are part of its supply chain. This means that if direct exporters number roughly 8,000 companies, the indirect exporters (suppliers of the above) would total about 40,000 companies.

Table 3.2. The Chilean Exporting Firms: Number, Size, Exporting Values and Continuity as Exporters

Años	Total Numer of Actives entreprises (IRS)	Exports at current values (BCCH-Millions FOB USD)	Exports at real values** (Millions FOB USD Year 2000)	Real value index (WB)	Number of Exporters (NCS)			Number of Enterprises that export < 5,000 USD	Number of Entreprises that export > 5,000 USD	Number of Entreprises that export more than 50,000 USD and less than 10 millones USD	Number of Entreprises that export more than 10 millions USD and less than 100 millones USD	Number of Entreprises that export more than 100 millions USD	Entreprises that does not export year before	Entreprisse taht does not export this year	Permanet Exporters (More than ten years)
					Total	Exporters (Enterprises)	Exporters (persons)								
1990	426.341	8.177	7.709	43,60	4.102	3.736	366	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
1991	443.265	8.690	8.222	46,50	5.349	4.040	1.309	1.120	4.229	2.246	n.a.	n.a.	1.382	1.078	n.a.
1992	465.790	9.757	9.212	52,10	5.445	4.122	1.323	957	4.488	2.448	n.a.	n.a.	1.329	1.247	n.a.
1993	489.264	8.972	8.470	47,90	5.496	4.486	1.010	998	4.498	2.463	n.a.	n.a.	1.463	1.099	n.a.
1994	532.792	11.301	10.680	60,40	5.844	4.530	1.314	1.033	4.811	2.660	n.a.	n.a.	1.343	1.299	n.a.
1995	554.238	15.655	14.747	83,40	5.817	4.636	1.181	982	4.835	2.706	n.a.	n.a.	1.460	1.354	n.a.
1996	581.901	14.816	15.313	86,60	5.839	4.704	1.135	1.112	4.727	2.687	n.a.	n.a.	1.419	1.351	n.a.
1997	585.626	15.955	16.444	93,00	5.754	4.789	965	1.026	4.728	2.756	n.a.	n.a.	1.424	1.339	n.a.
1998	653.303	14.457	15.030	85,00	5.840	5.018	822	1.063	4.777	2.777	n.a.	n.a.	1.541	1.312	n.a.
1999	659.696	15.663	15.790	89,30	6.069	4.823	1.246	1.134	4.935	2.860	n.a.	n.a.	1.343	1.538	932
2000	673.697	17.682	17.682	100,00	5.676	5.068	608	959	4.717	2.773	203	23	1.580	1.335	1.001
2001	685.668	16.964	16.815	95,10	6.024	5.163	861	1.087	4.937	2.842	204	21	1.556	1.461	1.042
2002	705.302	17.054	16.727	94,60	6.188	5.475	713	1.222	4.896	2.775	195	26	1.737	1.425	1.091
2003	716.479	20.294	19.945	112,80	6.435	5.712	723	1.296	5.139	2.924	205	34	1.723	1.486	1.160
2004	722.590	31.143	29.935	169,30	6.640	5.826	814	1.272	5.368	3.116	246	37	1.706	1.592	1.230
2005	748.064	39.543	37.981	214,80	6.880	5.951	929	1.332	5.548	3.137	262	46	1.713	1.588	1.279
2006	762.813	56.430	54.018	305,50	6.973	6.489	484	1.210	5.763	3.310	282	58	2.075	1.537	1.345
2007	772.223	65.379	62.276	352,20	8.157	6.747	1.410	1.558	6.359	3.561	305	64	2.058	1.800	1.401
2008	783.014	63.082	61.162	345,90	8.240	6.502	1.738	1.532	6.708	3.797	365	72	1.774	2.019	1.443
2009	782.203	51.239	47.830	270,50	7.519	6.566	953	1.156	6.361	3.537	317	60	1.880	1.816	1.520

Source: Author´s elaboration based on Data Bases of, IRS, NCS and DIRECON, 1990-2009. Figures in USD year 2010.

Confirming the above expressed assessment, we can see in Table 3.2. that the National Custom Service figures show that in the end of analysed period (2009) the largest exporting companies are those that yearly exported more than 100 million dollars (in 2009 were a group of 60 companies), explaining 72% of exports (Direcon 2010). Those companies, whose focus is essentially placed on foreign markets, are a relatively small group. In fact, the companies that have exported during a continuous period of ten years were only 1520 by the end of 2009. Thirty-three of these firms are large mining companies.

The concentration of export firms is evident, even though their composition by activity varies widely according to sector and size. Between years of 2000 to 2009, firms exporting more than $100 million dollars a year incremented their numbers by 161% (Table 3.2); nevertheless, the number of firms that export between five thousand and one hundred million dollars have not incremented beyond 56%.

In Chile, openness has been associated with a high concentration of export quantum and value in large companies, and even when the number of products exported by small exporting companies contributes significantly to the diversification of the exporting basket, but their participation in the monetary value of exports, in 2009, was marginal (Figure 3.7). Over the period 1990-2009, large exporters almost quadrupled their number, and middle-sized exporters doubled, but the number of small exporters increased by only 60%, generating only slightly less than 1.5% of the total value of Chilean exports. On the other hand, within the group of 73 largest exporters which deliver 78% of Chilean export value and, ten mining companies and two producer-exporters of cellulose account for almost 53% of the total value of the exports for the year 2008 (NCS-DNA 2010).

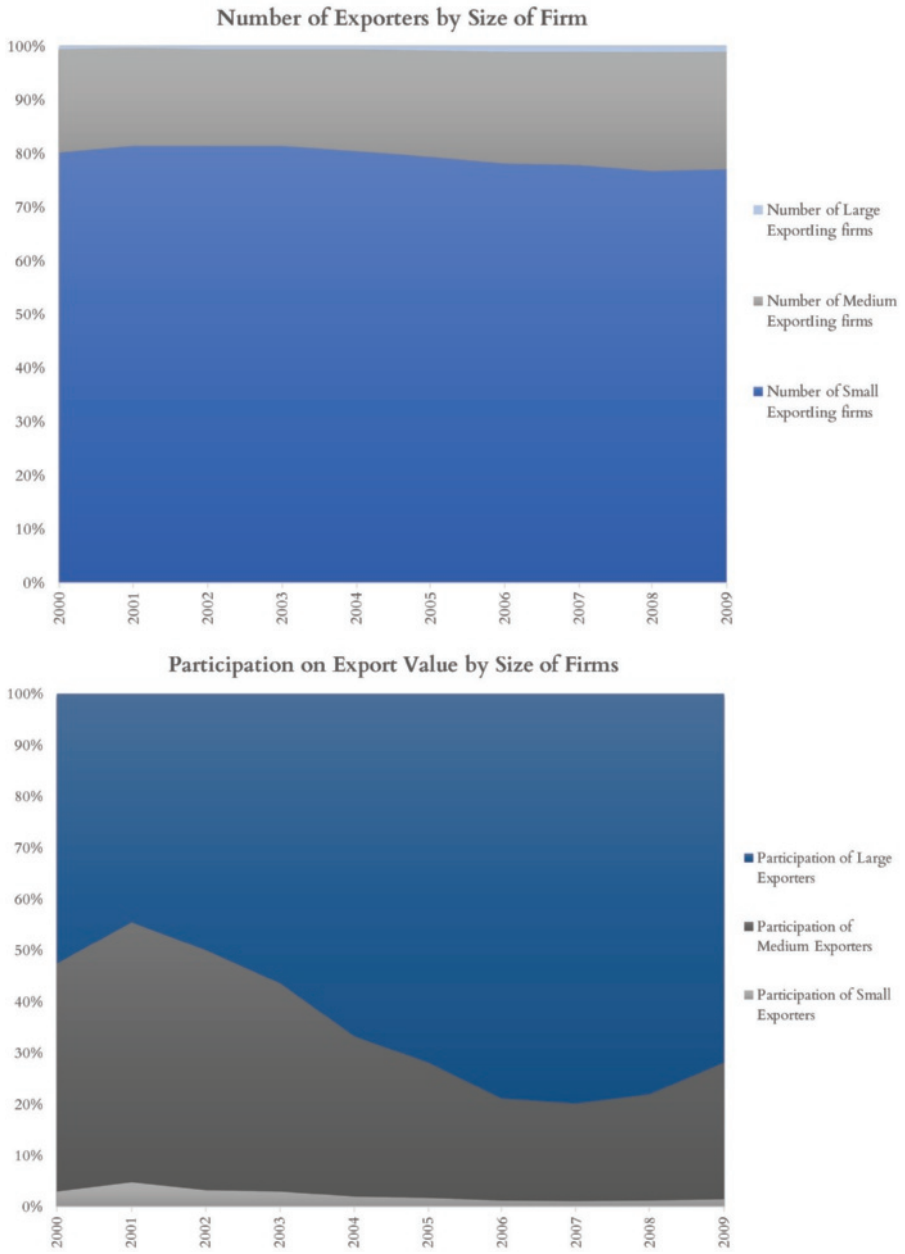

Figure 3.7. Composition of Export Sector by Size of Firm.

As we will be discussed later (Chapter VII), there seems to also be a strong dynamic of subcontracting and integration of companies within hierarchical networks. While, in theory, the Chilean economy is completely open and the export option is also

open to all companies, of any size, the number of small exporters tends to decrease. These firms also become increasingly smaller and tend to be integrated as indirect exporters, words, as suppliers of large exporting firms. The Ministry of Economic Affairs of Chile reported towards the end of the period under analysis (OEME, 2007), that 5.2% (39,667 firms) of the total number of formal enterprises of Chile (772,590 firms) operated as subcontractors of large export companies, suggesting presence of strong institutional boundaries to the operation of small-sized exporters.

The arguments which, from the neoliberal side are argued to this respect basically seem to be, that there are strong economies of scale in export activity. However, it is possible to point out that that situation does not appear to constitute an obstacle to the growth of small exporters in the Asians countries, whose major difference with Chile seems due to the institutional framework within which Asian exporters businesses operate.

The situation is quite different to Chilean LSE exporters. During the period under analysis, the value of Chilean exports in US dollars grew eight times and real GDP almost tripled. However, the gigantic scale of this wealth creation for the economy has not resulted in an equitable level of prosperity among the different economic actors; on the contrary, it is clear that export benefits derived are concentrated in a tiny group of corporations.

In general, is argued that one of the main reasons for the limited distribution of the benefits of foreign trade is the extreme concentration of exports in a few firms (Goldberg and Pavcnik, 2007. However, the Chilean case seems to correspond to levels of concentration higher than worldwide standard because export process not only involves a small and decreasing number of business, but also a lesser number of products, concentrating mainly in commodities with low added value.[87]

Institutional environments analogous to the Chilean one, in which exports are concentrated among a few large corporations, have been identified as dangerous and undesirable in recent literature.

Authors such as Parente and Prescott (1999, 2004) stress the role of monopoly power as a barrier to the adoption of technology by the economy as a whole. Other authors, such as Gali and Zilibotti (1995) and Rao (2006), suggest that high levels of economic

87 The quantity of products that Chile exports has fallen steadily from 5302 in 2005 to 4938 in 2010, but three or four mining products account for almost 60% of total export value (NCS-DNA, 2012).

concentration can cause underdevelopment traps. Acemoglu et al. (2002) and Benabou (2004) show how a lack of competition can reduce innovation. Acs and Audretsch (1988) present empirical evidence that concentration and innovation are negatively related and higher levels of economic concentration can lead to greater economic volatility.

As a result of the trade openness, exports have become the engine of the Chilean economy, but the growing share of exports in GDP will not necessarily provide an automatic transmission channel for the externalities resulting from the exposure of local companies to external competition (Holland and Porcile, 2005).

As we'll discuss later, the roots of this phenomenon appear to be of institutional origin. This situation is essentially produced by the fact that there are few Chilean firms directly exposed to foreign trade and the number of firms effectively involved in export activities, directly and indirectly is extremely reduced and hardly to quantify.[88] However, it is not entirely clear what has been the final cause of that situation of ineffectiveness of trade openness in exporter performance of Chilean firms.

Have changes in the relative prices not been enough? Or, have the institutional changes, both at the level of major rules of the game as on the area of specific institutional arrangements which define the operation of markets, not been operating in the right direction? Given that situation, before we analyse this crucial issue, it is necessary that we discuss in greater detail the real influence of trade liberalization on the Chilean business fabric.

88 The real incidence of Chilean openness in ensuring a real exposure to international competence and technological diffusion is, however, difficult to quantify. The research undertaken in this regard (Marshall, 1992; Rojas et al. 1997; Tybout et al. 1991; Alvarez, 1999) is not always based on good quality statistics. This is because they do not show, in a precise way, the real capacity of the external sector to generate exporting linkages, not only to the economy as a whole, but more specifically with different sizes and sectors of economices.

3.5. The Trade Openness Influence over Chilean Exporting Firms Performance

The weakness of the export focus of Chilean corporations can be appreciated through the estimation of the weight achieved by exports within the actual level of overall economic activity, measured using "export coefficients".[89]

Export Coefficient (EC) is defined as the relationship between the amount exported by each company and the total sales produced by them (Table 3.3). Firms with an EC of 1.0 are those completely oriented to foreign markets and they do not sell in internal markets. On the contrary, firms with an EC of 0.0 are those that do not export at all and are only oriented to domestic markets.

Table 3.3. Export Coefficients: Chile 2006-2008

	2006		2007		2008	
Export Coefficient	**Number of Exporters**	**Share**	**Number of Exporters**	**Share**	**Number of Exporters**	**Share**
0.0 – 0.2	2.957	57,0	3.304	53,4	3.663	54,9
0.2 – 0.4	590	11,4	690	11,2	731	11,0
0.4 – 0.6	476	9,2	570	9,2	571	8,6
0.6 – 0.8	503	9,7	560	9,1	489	7,3
0.8 – 1.0	659	12,7	1.063	17,1	1.215	18,2
TOTAL	5.185	100,0	6.187	100,0	6.669	100,0

Source: DIRECON, 2010.

Within this group, those, which are oriented to foreign markets, are predominantly mining and cellulose companies. In 2006, about 68.4% of exporting firms (the first two rows after the titles) had an EC lower than 40%, and in 2008 a 66%. Therefore,

89 In Chile, data on import and export rates is registered by the NCS-DNA and made available each year. They aggregate data at the economic level and include transaction details as well. However, data about internal sales of each companies are only confidentially registered by the IRS for its own use, but are not public because it's are covered by the Chilean Tax Privacy Laws. Since the crossover of both databases could damage the confidentiality of the information, the IRS only has made those cross overs at request of some authorised public institutions. The information quoted here was made available by the IRS only for the "Dirección de Relaciones Económicas de la Cancillería" (Direcon, 2010) is referred only to three years and is the only information available to date.

we can likely conclude that the main destination of their production tended to be the domestic market. In the higher rank of companies, composed of enterprises whose exports in 2008 were more than 80% of its total sales, (i.e. with a variable EC between 0.8 and 1.0 in 2008), we can only find 1215 enterprises (18.2% of the total).

At the other end of the distribution scale, where companies possess a very low EC, (firms that in 2008 exported less than 20% of their total sales), and their number ascends to 3663 companies, i.e. 54.9% of the total. In other words, the EC is relatively low in more than half of the Chilean export firms.

In half of the country's companies, shipments abroad represent less than one-third of their total sales.[90] Only the large Chilean companies specialising in export commodities have an EC bigger than the EC of all the other companies with shipments abroad (Direcon, 2010). In fact, if we exclude the variation produced by the rotation of exporting companies, and focus our attention only on the tiny group of larger 100 enterprises exporting commodities, we can see that they account for the bulk value of Chilean exports (81.2%). Then, it becomes obvious which the Chilean exporting sector has not been impacted by trade openness in the way that neo-classical and neo-liberal analysis assumed that it would happen.[91]

If the opening has failed to give the Chilean economy greater export dynamism and has not produced "right prices", it means that neither institution has contributed to instil a superior performance in Chile's economy. Then the crucial question about that is:

Why neoliberal reforms do not appear to have installed in Chile a price system and new institutions that encourage the firms' focus on the domestic markets, despite the drastic trade openness?

The answer seems to be on the weak and asymmetric orientation of Chilean firms to foreign markets, a fact that can be appreciated by observing Figure 3.7.

From there, we can draw three conclusions.

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90 It is interesting to note that if we look at only those companies in 2009, which permanently export with shipments higher than USD100,000, they account for about 72% of the total value of exports and 92% of the direct employment produced by exports.

91 This point has been stressed even by some World Bank analysts (Khanna and Palepu, 2000).

- Firstly, the evolution of the external sector in Chile is in the hands of a small clique of about thirty business groups (mainly but not only mining companies) that control the hundred companies referred to above.
- Secondly, the before described situation is not only referred to the number of larger exporters, but rather to the export´s value that is also extremely concentrated.
- Thirdly, economic openness has not been able to generate price signals that change the specialisation of the economy or orient the export activities of the bulk of the companies operating in the country.

For all these reasons, the Chilean economy continues specializing in commodities exported by larger firms and that are financing the existing deficit in the area of internationally tradable value added products.

The role of free trade agreements (FTA), which has been aligned within the original trade openness strategy, has not solved any of these issues. FTA only ensures the constancy of the foreign investment, the regulatory framework and the rights of intellectual property of large foreign corporations that have widely invested in Chilean markets, mainly in the mining, retail and utilities sectors.

3.6. The Employment´s Reallocation from the MSME to Large Scale Firms

From the neoclassical perspective, a labour migration from the MSME to LSE was exactly the expected result. There is a long tradition in economic analysis based on this view (Rostow, 1960; Fei and Ranis, 1964; Jorgenson, 1967, 1969; Harris & Todaro, 1970; Ranis, 2003, 2004) which assumes that economic development only can occur in two-sector economies through mechanisms of labour absorption from the backward sectors towards the sectors of higher productivity.

Applying this view to the Chilean case, this displacement can be seen as corresponding to what neoclassical models identify as a regular development process. However, the labour reallocation from the low productivity sector to the modern one is not autonomous; it depends on wage incentives that promote migration from one sector to another, and this is by no means a secondary consideration.

The employment produced by large companies from 1990 to 2009 (754,916 jobs) was 52% of the total employment produced during this period within the Chilean economy (1.44 million jobs) and 72% of formal new employments produced in the economy (1.05 million jobs). If we assume, from a neoclassical point of view, that wages correspond to the value of the marginal product of labour, we must also assume that, given that less productive labour is reassigned to sectors that generate higher marginal productivity value, they will receive higher wages.

Then, it would follow that, as Figure 3.8 shows, the replacement of precarious employment usually produced by SMES, or by the informal sector, would be produced through the generation of modern and better-paid jobs in the larger enterprises sector.

If we can demonstrate which that neoclassical hypothesis is coincident with the reality of the Chilean labour market, we would probably be in the presence of a growth pattern that would justify the neoliberal development strategy selected in Chile. Additionally, if such a situation were consolidated, by the presence of a constant replacement of traditional and bad paid jobs for modern and well remunerated ones, this would suggest we are in presence of a situation in which the country's income distribution would also improve in a slow but constant manner.

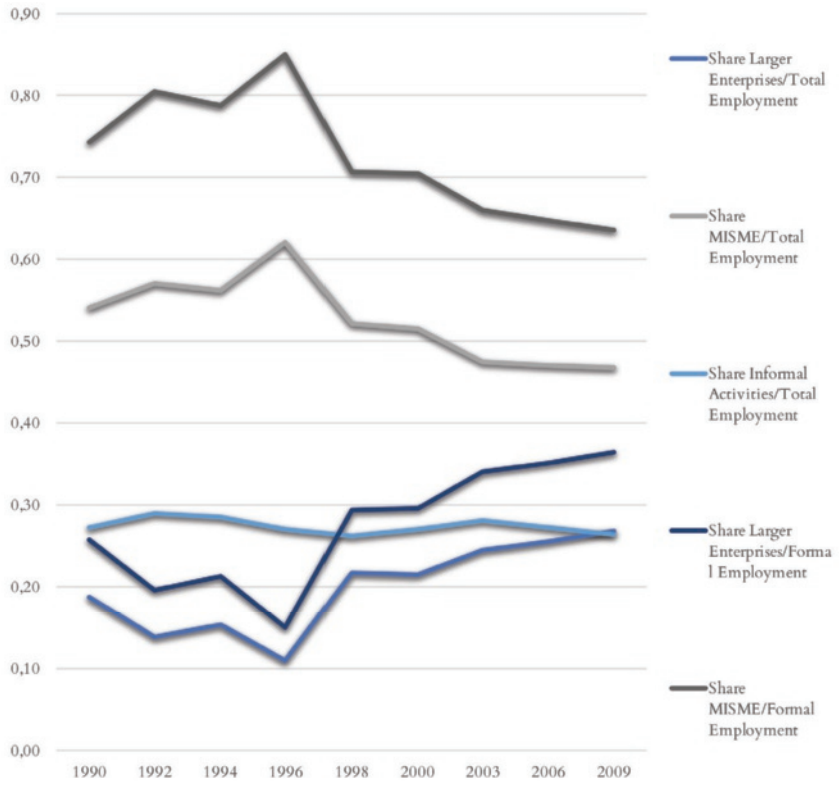

Figure 3.8. Employment Generation by Size of Enterprises. Chile: 1990-2009
Source: Author´s elaboration based on Surveys CASEN 1990-2009.

Nevertheless, the situation in the Chilean labour market apparently differs from the neoclassical hypothesis in two essential points:

- First, the quality level of the new jobs created by large enterprises does not seem to be substantially better than the quality of those jobs formerly produced by the MSME, (Henriquez et al., 2006; INE, 2011).[92]
- Secondly, wage levels do not show a significant improvement in the "modern sector" when compared to the "traditional sector". (ENCLA, 2002-2008).

92 During 2010, the Chilean economy created 487000 new jobs (INE, 2011). However, according to data from the New National Employment Survey, in Spanish Nene (NENE, 2011), 43% of the new jobs produced in the last year relate to self-employed, unpaid family workers, domestic servants or workers employed in enterprises with less than five people, in other words those who represent generally lower paid and unprotected labour.

More than any differences between "modernity" and "traditionalism", Chilean enterprises show productivity differentials associated with the level of technical progress embodied in each one of their sizes-strata. However, despite the radical nature of the opening and liberalisation of its markets, the situation of the remuneration of companies by size seems to be scarcely correlated with the level of technical progress of their productive processes or with their scale of production (Levisohn, 1999; ENCLA, op. cit.).
This assessment appears legitimate, but at the moment, we shall confine ourselves only to suggest, once more, that in labour markets seem to operate institutional determinants whose weight exceeds the influence of relative prices, seen as an expression of the value of the marginal productivity of labour. However, that hypothesis requires a more detailed analysis of the operation of the Chilean labour markets and their remuneration structures.

3.7. The New Labour Markets Institutions

Different analyses of the Chilean labour market (Alvarez and Lopez, 2004; Infante y Sunkel, 2009), have maintained that the elements which determine the low productivity of the Chilean economy do not seem to be due to the residual defects of the development model followed by Chile. On the contrary, low productivity seems to be linked to the main elements of the Chilean Model crystalized in some institutional arrangements who consolidate that situation (Infante y Sunkel op. cit. 59-61). These arrangements would be the origin of low levels of productivity growth and produce a dynamic that does not seem to follow the path of improvement that various authors argue such a phenomenon should generate in an open economy (Mankiw et al., 1992; Barro, 1996, 1999; Bergoeing et al., 2002; Paus, 2003; Paus et al., 2003).

The state of affairs in the Chilean labour markets shows that, at an aggregate level, the ranks of remunerations paid by each stratum of firms, are highly independent of their levels of productivity. It is highly possible that salaries are, therefore, determined according to different variables. Such as the market share of each stratum of companies and the level of market power of each enterprise both variables highly depending of institutional variables.

If we analyse the empirical situation of remunerations in Chilean labour market displayed at Figure 3.9, is possible to observe that, within the last years of our period of analysis, their performance seems to follow the before described situation, clearly

associated to contexts which are not characterized by a synchrony between evolution of wages and productivity.

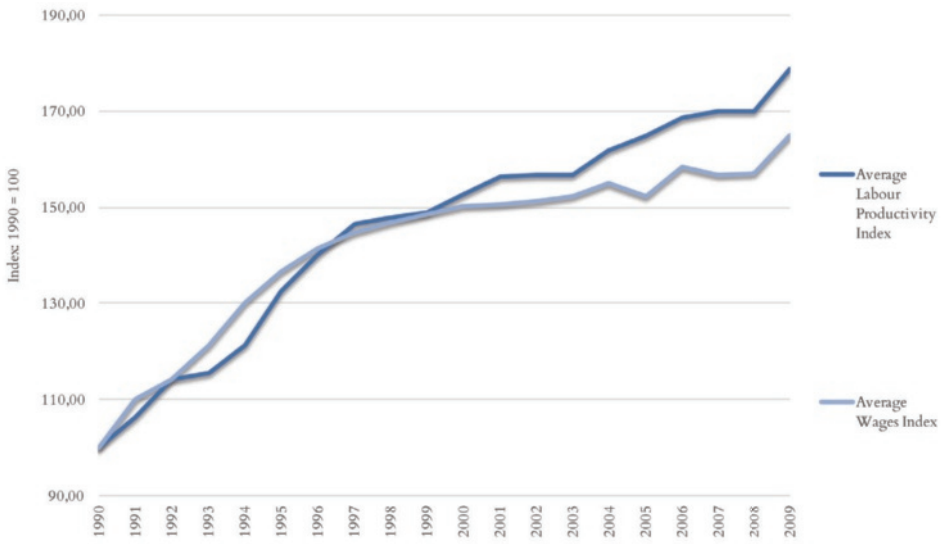

Figure 3.9. Evolution of Labour Productivity and Average Wages 1990-2009.

The trade openness has not introduced significant changes in that situation. As can also be seen in next Figure 3.10, which display situation of average wages existing in the three strata of enterprises of the Chilean economy. In that figure, we can see that on average, a dependent worker in Chile generates a little more than 1,7 millions of Chilean pesos each month (around 26 thousand Euros) (ELE-INE, 2015). However, there are sectors where this contribution drops to 14 million (manufacturing) or rises to almost 21 million (electricity-gas-water). By size of company, in general, a worker in the microenterprise generates a value of 1,3 million pesos per month, while in the large company this contribution rises to 6.6 times that value and reaches 7 million.

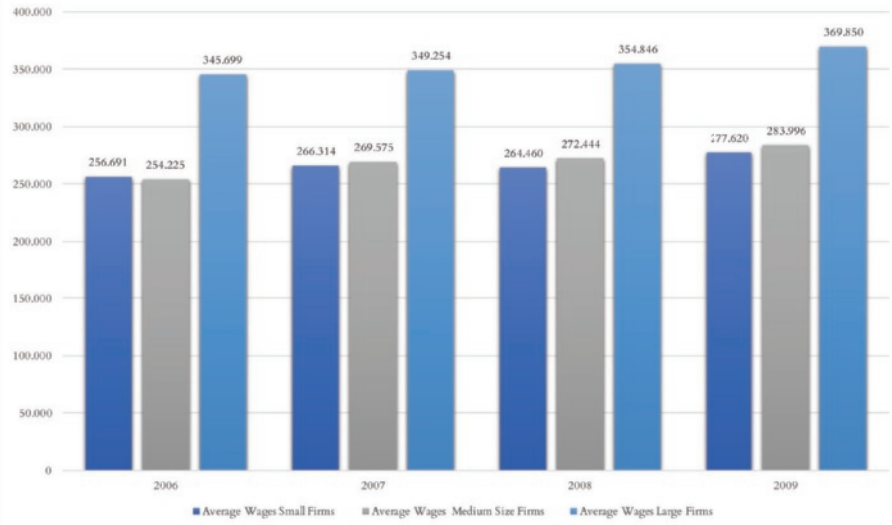

Figure 3.10. Real Wages by Size of Enterprises
Source: Author´s elaboration based on data from INE: 2007-2009. "Encuesta Trimestral de Costo Laboral".

Moreover, as can also be seen in Figure 3.10, even though productivity differed, there is only a very small gap between wages paid by MSME and wages paid by LSE. In fact, according to the official figures provided by the INE (2007-2009), the salary differential between the MSMEs and the LSEs is around 33% (approximately 100 euros per month), an amount that constitutes only a minimum small part of the differential (of the order of 7000 Euros per month) existing between the average productivity of an MSME worker, in relation to the productivity of a worker of large companies (op.cit).

Figure 3.11. Annual variation rate of total labour cost according to company size (at prices of 2009) Source: Author´s elaboration using INE data.

This situation of drastic divorce between the Average Labour Productivity and the remuneration of the workers, seems to be associated with the great market power that, during the two decades analysed in this research, have reached the big companies, supported by the institutional environment. It is not, however, only the presence of differences in the absolute values of remuneration, however small they may be.

The general tendency of the wages between size of companies, shows an important convergence between the values to pay for each stratum. In Figure 3.11, can be observed that the variations in the growth rates of wages (measured monthly), converge systematically towards single values in the case of large and medium enterprises, while smaller companies show wage growth rates greater than those of companies with much higher productivity. This situation, as it can be seen in this figure, is projected well beyond the period analysed. environment inherited from the dictatorship and by the new institutional arrangements settled by the governments that succeeded it.

During period 1990 to 2009, the large corporations had been capturing a market share which, towards the end of the analysed period, amounted to 84% of the total sales of the economy, giving employment to about 27% of the total workforce and

about 50% of formal sector workforce. In this regard, its ability to define levels of wages in a way that is independent of the productivity of their employees has been rising parallel to their rising market power.

At the root of the power which allows larger corporations to define salary levels within the economy, we can find the institutional framework in which they are acting. That framework was not spontaneously created. Before the Asian crisis, the macroeconomic policies were nominally neutral in relation to any size of firms or economic sector.

After 1997, the rules of the game that begun to be expressed throughout macro and microeconomic policies changed drastically, becoming highly discriminatory in function of the size of firms. The new vision of economic dynamics held, sometimes explicitly and in others only implicitly, that, given the Chilean economy's dependence on the performance of its large economic groups, economic policy should be oriented to empower them, since the heart of the "modernity" induced by the trade openness was rooted in them. Based on this new vision of the authorities and their associated actions, large business groups took control of the bulk of the markets and especially of the labour markets.

When we try to explain this situation, our only option is to look beyond the neoliberal-neoclassical framework. Evidently, the relationship between economic growth and structural changes in the labour market induced by trade openness and market liberalisation was not mediated by a wage structure depending on marginal productivity, nor did monetary wages act as a variable that permitted the reallocation of labour from low productivity sectors to more productive ones.

For all these reasons it is clear that the neoclassical and neoliberal predictions, assuming that the trade openness and liberalization of markets would produce increased competition levels in the Chilean markets, do not seem to adequately account for the behaviour of the Chilean labour market. Labour reallocation, in same way, has contributed to productivity growth (Vergara y Rivero; 2006; Ruiz-Tagle, 2007), but its magnitude has been very small and not been related to the dimension of changes in relative prices (Vega, 2007:200-207). Therefore, reallocation has not produced a proportional improvement in labour remuneration across sectors and sizes of enterprises, a situation that portrays an important disconnection between the evolution of productivity and wages.

Neoclassical economic theory assumes that, at the level of the firm, the total wages paid to workers would be equivalent to VMgP of the last worker hired in each company, multiplied by the total number of contracted workers (Hicks, 1932; 1989). Thus, in large corporations where there is a higher marginal productivity of labour, wages should be higher than in MSME (Berry and Mazumdar; 1991).

However, as we have already noted above, in Chile the wage differentials between sizes of companies do not seem to be associated with their marginal productivity differentials. If the neoclassical and neoliberal hypothesis was true and, after trade openness labour remuneration would be defined in an environment characterised by high levels of competition, then the proportion of well-paid workers should be lower in the more labour-intensive firms. MSME, especially those of smaller size, should be more labour-intensive and less productive whereas larger enterprises with higher labour productivity should be more intensive in their use of capital.

The reality of the Chilean labour markets has shown that, at an aggregate level, the level of wages actually paid to workers in the smaller or medium companies is associated to the value of their marginal productivity value more than in the larger ones (ENCLA 2002-2008; Minecon, 2014). Subsequently if remuneration does not depend on the factor's level of utilisation and associated productivity, and if opened was not in condition to align wages to productivity, it is sound to assume that the explanations must be linked to the specific institutional arrangement factors built in Chilean markets.

3.8. The Asian Crisis, an Inflexion Point

During years 1990-2009, they exerted strong influence over post-dictatorship governments, mainly by means of the implementation of macroeconomic policies and the installation of institutional arrangements which, after the Asian crisis, were utilised in Chile to reduce aggregate demand in the economy, adjusting it to the decreasing income levels induced by that crisis.

These policies cannot be explained by the intention of diminishing the global spending of the economy, which actually depend of the LSE spending and not of the MSME one. The contractive policies, operated through the rise of short-term interest rates,

favoured large companies because these were the only sector which, at that time, only had debts associated to long-term fixed-interest rates (Leiva et al. 2002).

The contractive public policies associated to the new policy approach of Chilean government 1994-2000, cannot be explained only based on the government's aim to reduce aggregate private spending, because the rise in short-term interest rates had little effect on LSE focusing only in MSME and in household expenditure, especially in the poorest household's expenditure.

On the contrary, it produced LSE consolidation as "premium clients" of the banking sector allowing, despite the recession induced by the Asian crisis, a fast expansion of their old levels of activity once home´s spending was recovered. The final result of those new policies was actually a significant expansion of the LSE market power.

The main victims of contractionary policies were undoubtedly the middle-sized companies, which in 1998 were in the process of expanding into international markets but had limited access to the credit required to do so. Because of the rise in bank interest rates, they saw their working capital disappear and had to adapt themselves to markets of smaller size, scarcity of bank funding and to a structure of low-wages induced by large corporations. This structure was taken by MSME as the best option available, given their scarce financial resources and the presence of productivity levels that were still insufficient to support a strategy of larger distributive significance.[93]

3.9. The New Institutional Arrangements in Labour Markets

From 1997 and afterward, the small, medium and micro-enterprises were forced to endure a severe restriction of resources. The most evident consequence associated with this constraint was the worsening of wages which, started to be forced down by large companies. Medium and small enterprises were obliged to adopt this new structure quickly to avoid disappearing from the markets. This situation did not improve once the Asian crisis finished, on the contrary, it has significantly worsened.

93 In the case of small and micro-enterprises, the situation operated similarly; even though it is known that they possessed productivity more than eleven times lower than of the big Chilean companies (Infante, 2011), it was surprising to see that their salary differences with large firms were only close to 30%.

Within the neoclassical framework, changes in the wage levels accompanying changes in GDP are necessarily associated with productivity changes across sectors or sizes of firms. From this perspective, the firms that are better skilled to act in response to external shock resulting of competition, are those able to develop solid improvements of their productivity.

This view assumes that the businesspersons aim to promote use of the highest quality productive factors within their companies; because of that, wages will tend to increases at the maximum levels that productivity improvements would allow. This upgraded supply would also generate a market share expansion of these companies, which would enhance their capabilities to attract even better quality production factors.

The impact of this new hypothetic resources allocation process may be characterised as a virtuous circle and would not only restricted to domestic markets. Companies that improve their productivity come to be internationally more competitive, hence they will tend to gradually improve their export capacity, absorbing in that way the negative impacts of price shock associated with openness.

However, this virtuous cycle described by the neoclassical narrative, is based on the presence of a specific mechanism enabling this evolution: the existence of a close and positive correlation between productivity and wages at the firm level.

If this correspondence is not created and the markets remain operating in a context of imperfect competition, this will generate economic rents to be appropriated by capital. Such rents shall be equivalent; ceteris paribus, to a given level of hired labour force, the difference between the salaries paid to workers and the minimum amount necessary that the company must have to be able to hire such workers (i.e. the value of labour remunerations), will be determined by the elasticity of demand for labour, or regarded in a broader way, by negotiation´s capabilities that workers must deploy.

When, in the real economies, companies with greater market power and that concentrated the bulk of labour supply are in position to reduce the value of real wages in a joint way to its market control, the companies that challenge their power should compete very hard to avoid being displaced from their traditional markets.

For them, weakening of remunerations becomes an imperative for defiant (mainly the labour-intensive companies) since otherwise their prices would prevent them from

effectively competing. When input and output markets are highly controlled by greater market power companies, the wages become thereby the adjustment variable easier to use by companies with weak or no power market. In that way, the companies that control the markets become the ones who define the wages values, transforming the companies subject to their power in mere price takers in each one of the markets in which they operate.

This is a situation in which markets, far from approaching to a competitive context, tending to move increasingly away from that environment. Therefore, it is not easy, in practical terms, to associate the trade openness to the installation of an efficient allocation of resources in the economy. At least not one that would approach- as neoliberal assume presence of perfect competition, or at least significant competition.

3.10. The dynamics of wage setting by large companies

In Chile, the work force of the formal sector, is distributed, by almost equal parts among the LSE and the MSME. This means that both business segments compete to capture the best elements of this labour force (that is, the most productive). Assuming that the wages offered to them by the companies are the variable around which the allocation of labour takes place.

The expected result, then (according to the neoliberal hypothesis), would be that the LSEs require more productive, more modern and efficient workers, capable of adapting to their productive or commercial processes. By offering them higher wages, these companies would attract the best workers. Thus, an upward effect on market wages would be produced, which would force the backward companies to improve their productivity to finance those higher salaries that facilitate their access to qualified resources on which they should sustain their competitive strategies. However, reality seems to have gone the other way.

Figure 3.12. shows the salary level determination dynamics that regulates the relations between the two strata of companies (LSE and MSME).

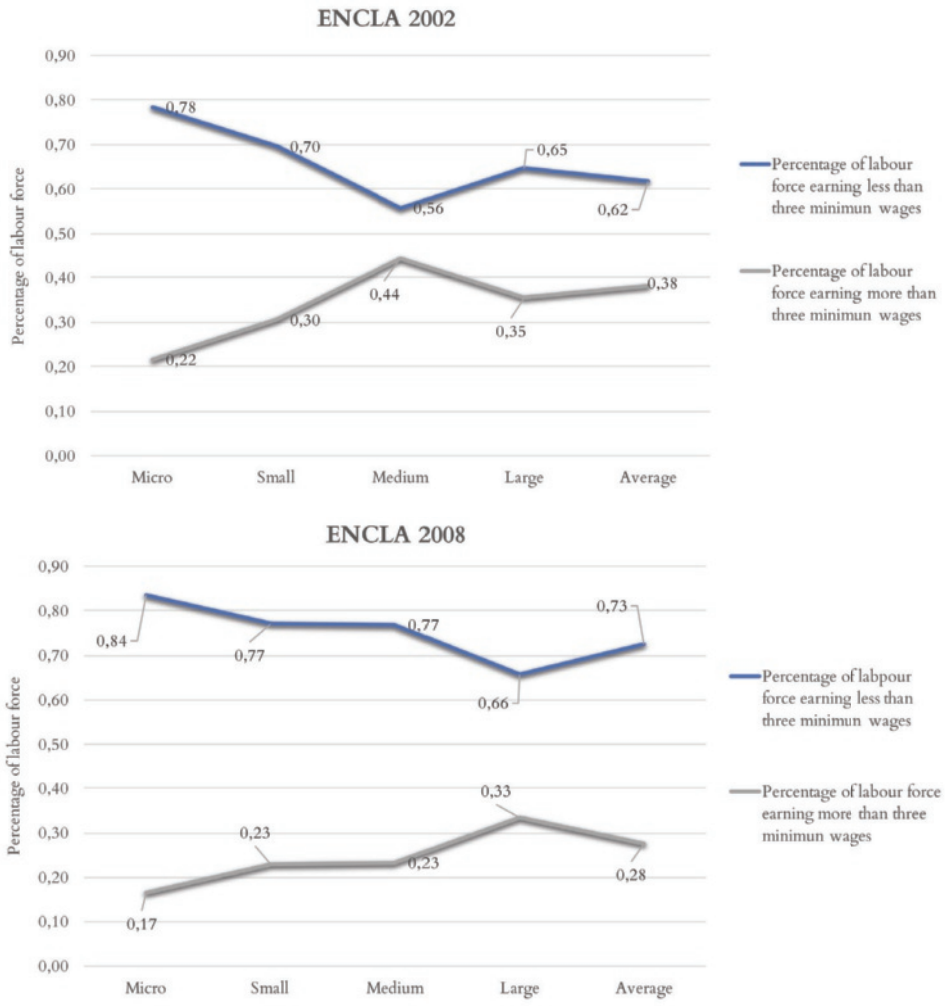

Figure 3.12. Wage Structure by size of Enterprises.
Source: Author´s elaboration of microdata from National Labour Survey. (ENCLA): Chile 2002. 2008. Ministry of Labour.

Comparing both sides of figure 3.12. (2002-2008), we can observe that the wage structure, as a whole, had worsened (after 2002) due to actions originated in the LSE sector. Thus, we can see in each strata of firm size, what percentage of hired workers who earn less than three basic salaries (the basic OECD wage). This tendency to hire cheap labour may be visualised with more intensity in small and middle-sized companies, but, as a result of heavy influence of LSE on labour market (they define the "floor" of high salaries and the "roof" of low salaries, pushing down the salary structures of the economy as a whole), finally, in every size of enterprise the trend becomes the same.

The origin year (2002), 64,6% of LSE´s workers earned less than three times the basic wage (versus 66.6% in 2008). The same year 2002, 35,3% of LSE´s worker earned salaries bigger than three times the basic wage, (compared to only 33.4% in 2008). In both cases is showed a significantly lower level than that existing at the beginning of the analysed period.

That figures shows that despite a serious improvement in GDP, the general Chilean structure of remuneration seems to have deteriorated. In year 2002, 61.9% of workers in the country earned less than three basic salaries, but six years later, 72.5% of Chilean workers were placed below that level. This situation was obviously not anticipated, given that this was a period in which, at the same time as achieving an average GDP growth rate of 4.7%, the Chilean economy reached higher levels of trade openness and market liberalisation, consolidating an average tariff of less than 1%. However, it fell short on the promise of generating an improvement in wage structure, so that Chilean wages levels approximated international values (vis a vis productivity enhancements).

Figure 3.10 also shows that the wage structure has clearly worsened across all strata. In fact, in 2008 all sizes of enterprises hired a higher proportion of employees who earned less than three times the minimum wage, and a smaller proportion who earned more than three times the minimum wage, in relation to 2002. The red curve shows how many workers earning less than three times the basic wage have moved upward, while the blue curve showing how many workers earned more than three times the basic wage, has moved down. Each stratum of companies recorded a worsening of their wage structure. Even though this was more severe in small companies, it was nonetheless present in the rest of the strata, specially in medium size firms.

The percentage of large company workers who in 2002 earned more than three times the basic wage (35.3%) was at that time slightly lower than the proportion of workers achieving that wage level at a national level (38.2%). On the other hand, the percentage of large enterprise workers who in 2002 earned less than three times the basic wage was at that time 64.6%, a figure higher than the national average of 61.9%. This suggests that large corporations remunerated a lower percentage of their workers with high wages, in relation to the level at which the strata of smaller size and productivity did. Inversely, they remunerated a higher percentage of their workers with low wages than the other strata did.[94]

94 Detailed information provided by INE in its survey: Wages and Average Cost of Labour (2006-2009), also confirms ENCLA's information in relation to small wages differentials existing between sizes

In fact, Figure 3.13 clearly shows this; especially in the case of middle-sized enterprises, a stratum that in 2002 does exhibit better wage levels than the large companies and small enterprises. In 2008, however, it had already been unable to maintain these wage structures and had dramatically worsened them in order to compete with the low costs of large companies. On the other hand, the small and micro-enterprises only exhibit slightly worse levels than medium enterprises for some years, and average remunerations only 25% less than the large enterprises wages.

Following ENCLA figures, during 2002, Chilean middle-sized enterprises only hired 55.7% of its workers at levels lower than three times the basic wage, a statistic almost ten points lower than that exhibited by large companies (64.6%). At the same time, middle-sized enterprises remunerated 44.3% of their workers at more than three times the basic wage, compared to the 35.3% hired by large companies.

In summary, this means that, on average, 2002's salary structure was highly and progressively influenced by the remunerations of middle-sized companies. The other influential situation was that of small enterprises and micro-enterprises who hired respectively 69.5% and 78.4% of their workers with salaries of less than three times the basic wages, and 30.4% and 21.6% respectively with salaries over three times the basic wage.

These figures show that, when large companies reduce the number of workers with higher salaries (by lowering their labour costs), a wage roof is produced that depresses all remunerations. Given their lower productivity, companies of smaller size cannot compete with large companies while maintaining their relatively high salaries. In the same way, when the big companies lose their remunerations, there is an automatic limitation in the options of the workers. If they are not in a position to provoke wage increases in the most productive companies, it would be very risky to press for wage increases in small companies struggling for their subsistence. Even though in the past they had distributed a large part of their low profits through salary improvements, they are not able to do so now. The dramatic drop in the MSME sales share is a clear example of this, a situation that becomes clearer even when we consider that large enterprises possess an average productivity about 5,5 times higher than micro companies, 4,8 times higher than small firms, and 4,1 times than middle-sized do (Minecon, 2014).

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of enterprises.

Between 2002 and 2008, the Chilean economy was recovering from the Asian crisis of 1996-1998 and restarting the dynamics of its GDP growth, but these dynamics did not imply an improvement in the wage structure. Large firms that are more productive continued hiring more than 66% of its payroll offering remuneration inferior to three basic wages, imposing this wage structure on those strata (middle-sized enterprises) which, before the 2008 crisis, had higher wage levels. In fact, the "cheap-labour" strategy initiated by large companies undermined the salary position that the middle-sized employees previously had. The deterioration in the remuneration of middle-sized companies from 2002 to 2008 is difficult to explain from a neoclassical point of view. It is not typical that whilst undergoing the trade opening process, a vibrant sector of modern and productive middle-sized firms, should standardise their structure of remunerations emulating the cheap labour strategy of large companies (Henriquez, et al.; 2006). In fact, since 2008 the medium enterprises whose fair wage model harmonised with productivity development better than in large companies worsened their remuneration structure despite the presence of a vigorous evolution in the productivity of their workers (Minecon 2014).

3.11. The Neoliberal Governance of the Chilean Labour Markets

In our opinion, the inclusion of institutional factors as major determinants of wage structure is necessary. Without this institutional perspective, it is not possible to arrive at an adequate explanation of the performance of the Chilean labour market. If real GDP rose, the increases should be distributed in balanced way between the production factors, but that did not happen in Chile. On the contrary, we observe the absence of institutions that encourage competitive processes, ensure efficiency and let the market distribute wealth in a way associated with productivity. In our view, imbalances in the Chilean labour market are due to the pressure of large companies that seek to exploit the minimal labour market arrangements existing in Chile, which allow them to use various institutional tools in order to reduce wages.[95]

The two most important devices used by large corporations to reduce their costs are lower wages and the transferral of any economic risk to another company (subcontractors

95 The maintenance of low wages in the Chilean case was not achieved by means of macroeconomic measures but rather through institutional channels. The formula during the dictatorial period was prohibition of the right to strike and during the post dictatorship period this evolved towards the legalisation of industrial action, while maintaining the right of employers to hire replacements for the striking staff

and suppliers of a smaller size – MSMEs) implementing a kind of arrangement that the legislation of USA, EU and of other Latin American countries, would consider abusive or illegal.

Given that the initiative and power are in the hands of large firms, the resilience of workers and small employers is reduced, especially in times of crisis with high and persistent unemployment such as the Chilean economy faced after 1998, a period in which new institutional devices of neoliberal inspiration were implemented in a highly successful way.

The degree of labour mobility between sectors may be the key to understanding the functioning of the labour market. If there were labour mobility among sectors and sizes of firms, as the neoclassical version posits, in such a case, the theory of human capital would be appropriate to analyse the evolution of labour remunerations (e.g. Eyzaguirre et al.; 2005). Nevertheless, if mobility is restricted, as happened in the Chilean case (Ferrada, Ch. y G. Reinecke; 2004), the institutionalist theory of segmentation could provide better elements for analysis of labour market.

Generally, institutional analysis agrees that markets are organised in accordance with the existing institutional arrangements. In addition, it admits that the market is not the allocating mechanism of resources, rather it is the institutions and, especially, the power structures that organize markets; the markets, in turn, help to preserve these structures (Greif A., 2005). Following this line of argument, the situation of the Chilean labour markets is very similar to the one described by Bowles and Gintis (1986, 2002) who suggested that workers are assigned to different occupations and incomes, associated with different levels of productivity (primary and secondary), for purposes of social stratification and control.

In the Chilean case, the secondary sector may be associated with MSME. In that sector, there are few obstacles to labour mobility, but there are also few incentives for job retention, so there is a high level of turnover (people change employment or company with ease). Salaries are low (in absolute terms) and working conditions are not good. Belonging to this sector depends in large part on the social class of the parents of the people who are assigned to this sector. Education operates as a tool that has the primary function of legitimising this structure of unequal reproduction through a facade of meritocracy. That is another institutional arrangement that produces segmentation in labour markets and hence enlarges the market power of LSE.

The large Chilean companies have segmented the labour market, clustering an increasing part of the workforce around a primary labour market, in which jobs are generally more skilled, better paid and more prestigious. This is the reason why LSE employers are those that offer the best conditions on the Chilean labour market (Parrilli, 2004).[96]

Thus, the segmentation induced by large companies (and governed by neoliberal institutions) extends to the whole of the labour market, even subordinating the educational system to this dynamic. In this way, the alleged meritocracy promoted by the noteworthy expansion of access to technical and vocational education,[97] has become, along with the trade openness, a core element of neoliberal discourse. Another important institutional arrangement which has promoted a new segmentation process in labour markets, is the massive integration of a vouchers´ system supported by loans from private banks with the guarantee of the State.[98]. In this way, the discourse about the merit based promotion and the improvement of human capital, that is heavily marketed, actually constitutes a mere discursive façade, given that there is no well-established link between education and market remunerations.

Those visions that stress the presence of labour mobility and human capital improvements, divorced from the wage determination process, appear to be in line with the real performance of Chilean labour markets as reported in research by Núñez and Perez (2007); Núñez and Tartakowsky (2009); Núñez and Miranda (2007). This research finds that the Chilean labour markets remain broadly segmented and present high levels of discrimination. Both factors prevent salaries from being based on productivity, instead associating them with forms of social stratification encouraged by higher-income groups with important social power.

We can conclude that the Chilean institutional environment and their associated institutional arrangements, involving new economic behaviour of individual and collective economic agents, are running inadequately. However, this is only true for

96 The already referred low work conditions and worse remunerations must be considered in relative terms. In LSE, wages are about 30% higher than in MSME and there not quantitative information reporting the meaning of worse work conditions existing in MSME.

97 It must be remembered that the Chilean educational system is highly privatised and integrated with private banking.

98 See: http://ciperchile.cl/2011/12/20/los-intereses-del-cae-%E2%80%9Cno-se-por-que-se-pagaron-a-los-bancos-sobreprecios-excesivos%E2%80%9D/

workers and small businesses, but it is not for the LSE who benefit widely from these arrangements. This means that the institutional rules governing the Chilean markets act in a positive manner for the LSE who define and impose these arrangements, but they are highly counter-productive for the economy and for the interests of the rest of the economic actors. All that variables are influencing the way in which the market´s competitiveness should be operating and starting from there, negatively affecting the outcomes of the development model.

In summary, the prevailing Chilean rules of the game seem to operate very differently from those defined by neoclassical economic theory and promoted by neoliberalism. Contra productive institutions prevail over effects of trade openness and market liberalization, lead labour markets to an institutionally defined set-up that, as we will show in the next chapters, may be harmful for economic growth and consequently to development, as has been reported in similar national contexts by Bjørnskov (2008).

3.12. Conclusions

The Chilean economy seems to represent a major challenge in analytical terms. On the one hand, it has great macroeconomic indicators, showing that it is achieving major success in the field of growth led by exports. Significant advances in the field of human development and quality of life indicators (UNDP, 2011, 2013) have accompanied the process of economic development. However, there are well-founded doubts about the distribution of the fruits of growth in function of the productivity of factors and about efficiency and sustainability of the growth process associated to the neoliberal model.

- The Chilean economy has failed in the field of value added generation, continuing its dependence on mining exports in a manner very similar to that which existed before the onset of trade openness and market liberalisation. Similarly, we have not seen further advances in the field of efficient resource allocation in the Chilean economy nor a substantial increase in the mobility of factors. Despite the drastic changes in the Chilean structure of relative prices, only minor factor mobility has taken place within labour and product markets.
- Our findings display a situation in which a change in relative prices neither induces changes in economic specialisation nor synergic relationships between firms and factors of production across economic sectors. Because of that, the neoclassical-neoliberal hypothesis can be considered, in the Chilean case, as

one without major explanatory capabilities. In that case, it would be necessary to explore whether the institutional hypothesis, which analyses the influence of the trade openness on the economy and on the current interrelations between market´s performance and the economic rules of the game (e.g. institutional environment and institutions of governance), may provide the clarifying potential that we are looking for.[99]

- This chapter showed that in 2009 in the Chilean economy only 10,174 firms, of the 782.203 thousand formal companies in operation, correspond to large corporations. They generate over 84% of the sales of all Chilean companies, showing a rate of sales growth, which increases each year. However, a small group of ten firms account for half of GDP, while the 73 major exporters account for 78% of the country's exports and nearly 20% of GDP. That evidence shows that 35 years of economic openness have had extremely modest results in terms of firms' export orientation and only a small number of LSE are fully oriented towards external markets. The rest seem to make use of their position in the internal markets in which they operate without a major level of competition and without being engaged in a significant effort at economic growth based on productivity.
- The LSE seem to behave in a way that is mostly refractory to the influences of the globalisation process in the economy, and only a small group of them have yearly exports of more than USD100,000. Chilean firms are weakly oriented to foreign markets, and only a tiny group of large exporters of commodities explained the bulk of Chilean exports. In 1990 Chilean total exports were 45.6% non-refined copper and 10.1% others mining products, but in 2009 those figures were 50.2% and 7.5% respectively, intensifying the cooper specialization of the economy. The core of the non-mining large Chilean enterprises remains focused on the internal market. That situation will not ensure that the Chilean economy benefits from the spread of technical progress coming from the external sector. Neither will it ensure the development of endogenous capabilities of generating technical progress.
- The new relative prices in the Chilean economy do not seem to have been able to reduce existing oligopolistic powers by means of introducing greater competitiveness into markets. On the contrary, the concentration appears to be higher than in the period prior to trade liberalisation. The specialisation of

99 This theme will be addressed in detail in the chapter VII.

the on-going economy, focused on the export of non-refined copper, continues to be very similar to the situation prior to trade liberalisation.

- Economic diversification produced by trade openness has been extremely weak and only focused in those sectors highly intensive in natural resources, with low value added, as well as highly intensive in cheap labour utilisation.
- Given the above, the Chilean economy presents a important level of concentration, as a result of which firms that are not controlled by large business groups (mainly MSME) have been losing much of their market share and the resources that would enable them to develop links to external markets. Without these essential elements, it has become increasingly difficult for them to develop endogenous capacities for productivity improvement.
- The figures related to the rapid growth of market share of large companies, the decline of the MSME, and reallocation of jobs towards large companies without development of a greater synchronization between productivity and wages, seem to show the dominance in the Chilean economy of a predatory business model. In this model, MSME participation in global supply chains seems to be critically blocked in terms of market access, building of progressive network governance and a sustainable chain upgrading. Moreover, given the impact of these phenomena, Chilean economic figures analysed together, would suggest that there are critical institutional issues explaining such blockage.
- The evidence reported here allows you to guess that the prevailing institutional arrangements in the Chilean markets play an important (but negative) role in the overall efficiency of the economy. These arrangements, understood as a set of rules, are important for the access of economic actors to relevant information that orient their decision-making processes and for the formulation of agreements on the terms of trade in a context of incomplete contracts. The existence of these rules of the game appears to have influenced significantly in the configuration of the Chilean markets, in its structure of action, levels of supply and demand, in the determination of prices, and the allocation of resources and the distribution of benefits among economic agents.
- The Chilean context does not seem to correspond to one in which the economy seeks to maximize levels of efficiency through minimization of transaction costs. Although quoted "adaptive efficiency" is that which allows incremental institutional reform in the more advanced representative democracies, the neo-liberal model of "semi-sovereign democracy" (Hunneus, 2015) seems to be placed quite far away from such a mode. Creation of mechanisms of negotiation and agreements´ definition between stakeholders, oriented to

reduce transaction costs, no doubt improve the efficiency of an economy. Therefore, the function of the organizations (firms and others) should be adopt the best structures in order to minimize transaction costs produced by collective action. However, this mix of hypothetical institutions, which rational choice-institutionalism thought seem to conceived as "pure public goods", does not have a solid empirical and historical basis in the Chilean case. On the contrary, it is common that domestic institutions become only "clubs" that favour certain economic actors, social actors, demographic groups, productive activities, etc. excluding other agents of their potential benefits. In the Chilean case, there is a clear predominance of institutions built during dictatorship and reinforced during the post dictatorship period. They seem to be aimed to the capture of economic rents and decoupling of processes for the improvement of economic efficiency in allocation of resources, production of goods and services of the Chilean economy. The set of institutional rules that should allow the negotiation between actors in domestic and international markets, seems to be severely constrained by the implementation of the neoliberal model. That model is associated to strong institutional barriers to any change in the rules of the game or in the institutions of governance of markets. However, all these issues will be analysed in the next chapters.

- We can conclude that in Chile the outcomes of trade openness and market liberalisation processes are far enough away from that forecasted by its promoters. The economy does not seem to be attuned with the scenario of export dynamism, raising innovation and widening of opportunities that was supposed must be opened to all sizes of companies, as offered by the neoliberal proposals. The bush-league performance of the Chilean exporting enterprises, the slow growth of the product and the contra productive kind of markets governance introduced by neoliberals in the Chilean economy; make it very difficult to assume that it will sustain in the future a dynamic of growth similar to that of their golden period 1985-1998. Based on that, we may conclude that, in the Chilean economy, changes in the system of relative prices were not capable to introduce the expected levels of efficiency; however, a deeper analysis of the institutional determinants of this problem will be developed in next chapters.

Chapter 4

The New Faces of the Chilean Model and the Elusive Process of Convergence

The objective of this chapter is to analyse the effects of trade openness and liberalisation on the convergence of product and productivity in the Chilean economy, trying to establish the degree to which this country is converging with more developed economies.

Based on observable outcomes, we assess whether convergence existed, but also, we draw conclusions about the reasons for its success or failure, in connection to neoliberal forecasts associated to the openness process used to promote the implementation of the neoliberal model. Here the concepts and debates around the convergence process are explored initially, in an attempt to explain the meaning of the concept, as well as the potential presence of this phenomenon, as it is associated with the trade openness and market liberalisation implemented by Chile. To test the existence of convergence in the Chilean case, a model of measurement is designed and applied, allowing comparison of the evolution of the Chilean GDP per capita with that of OECD member's countries. The concept of "conditional convergence" was used here, to analyse the success or failure achieved by Chile in the "conditionality" area, after application of the Washington Consensus' prescriptions. From that basis, we draw up an early assessment as to the extent to which the achievement, or lack, of convergence goals is related to institutional factors. Once elucidated this point, our investigation will continue clarifying if actually the real outcomes of the Chilean model are determined by changes in the system of relative prices or by the institutional fabric within that this model operates.

4.1. "Good-bye Latin America"

Chile belongs to a region that is characterised by its low growth. At the root of the Latin American low growth dynamics, seem to be the presence of a severe deficit in terms of productivity, as it registers Figure 4.1.

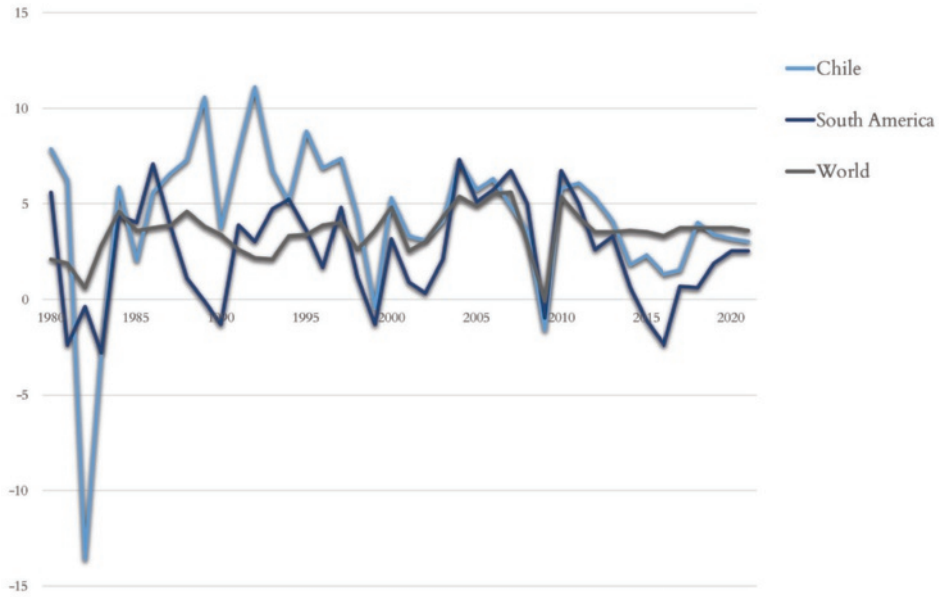

Figure 4.1. Compared Real GDP Growth

Even if data is included from the years during which Latin America has enjoyed a boom in its raw materials prices, the overall result of region is very poor both in terms of its GDP growth and in terms of its productivity dynamics (Easterly et al, 1997; World Bank, 2012).[100]

Within this context, the regional exception seems to be Chile, which grew far above regional average. The Chilean rate of growth presents prominence within Latin America but there a lot of discontinuities in that tendency. In fact, if between 1960 and

100 Lora and Pages (op. cit.:2) on the basis of Heston et al (2006), World Bank (2008) and Barro and Lee (2000); asses than if the productivity of Latin America and the Caribbean would increase at the same rate as in the USA, the per capita income of the region would reach a quarter of that country's per capita GDP. However, if the productivity of the region had been equal to USA, then Latin American GDP pc would have doubled, being in 2006, two-thirds of the GDP pc of USA.

2006, Chile had grown constantly at the same rates as the rest of the world (excluding Latin America and the Caribbean region), at the end of that period its GDP pc would have equalled those of Greece and Portugal (Pages 2010:37-47). However, this has not happened. The reason for this delay seems to be the low productivity of Chilean economy.

If we analyse the long-term tendencies of the GDP growth of the Chilean economy, we can see in Figure 4.2 that between 1960 and 1973 an unstable and near to the ground economic growth was recorded. However, starting from 1975 (once the neoliberal model was fully installed), the situation changes radically. From there onwards, despite the presence of successive external shocks, the Chilean economy jumped to higher levels than its historical patterns, arriving at certain periods to become the highest in the world. From the neoliberal perspective, as we discussed in the preceding chapters, this phenomenon has been attributed to the fact that Chile incorporated into its development strategy, markedly different principles from the rest of Latin American countries. Therefore, trade liberalisation, the use of the market as a key element of the allocation of resources, the minimisation of the role of the State and the export led orientation of the economy, would have been, according to neoliberalism, the keys to its success.

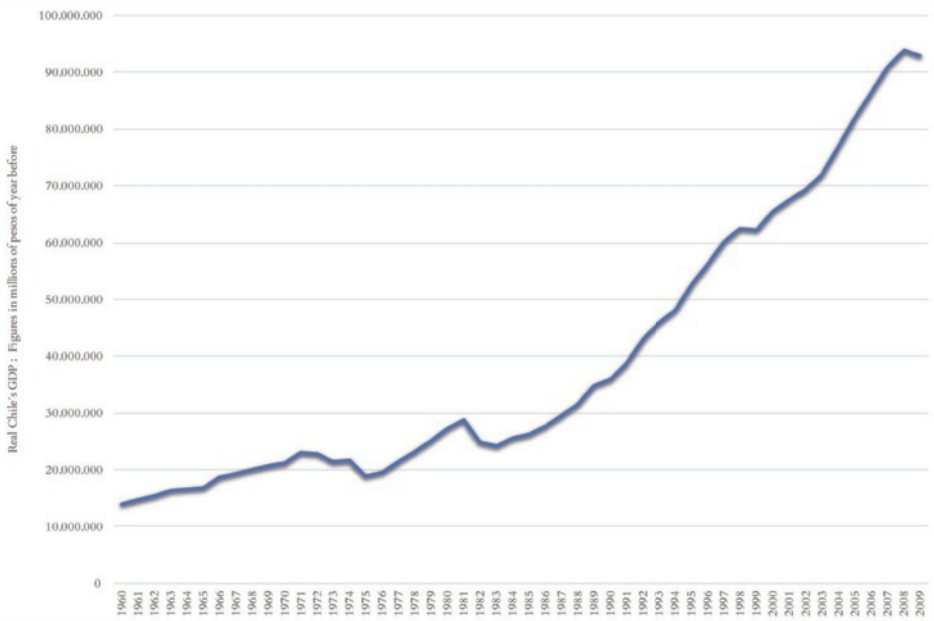

Figure 4.2. Chile's GDP growth: 1960-2019
Source: Chile´s Central Bank.

During the military dictatorship, period in which the Chilean model was installed, the deployment of a solid and stable process of economic growth was not a isolated neoliberal promise, but rather the "mother" of all neoliberal promises. In spite of this, in 1990, the outcomes that the model had promised were not only failing to be achieved, but were far from being achieved in the future. Between 1973 and 1985, Chile´s GDP had increased only 22%; however, the high rates of economic growth obtained by the economy from 1985 onwards (37% in just five years) allowed neoliberalism to maintain its augur of convergence as key point of their political promises. After long years of hardships, during the second half of the eighties the Chilean economy began to grow rapidly, while the rest of Latin America was struggling against successive crises, immersed within a period that was later termed the "lost decade" (Stiglitz 2003; Cepal, 2013). This particular context was used by the neoliberal discourse to promote ideas that made sense to many economists and politicians, even if some of them were located far beyond these conceptual boundaries.

Since the neoliberal speech, it was argued that Chile had followed a diametrically opposite path of the rest of Latin American countries. The country had opened its economy, deregulated its markets, privatised its public companies, reduced the level of their public spending and created a new Central Bank as an autonomous entity, preventing the Government from using money emissions to finance fiscal deficits. This, they stated, was the reason that Chile, starting in the 90´s, was growing at high rates, with balanced budgets and without inflation, while the rest of Latin America was experiencing crisis, hyperinflation and stagnation. That particular point of view had originated prior to the 90s. In the last years of the dictatorship a sentence was coined as a political slogan which pithily summarised what the Chilean neoliberal project understood as its main outcome: "Good Bye Latin America". In other words, the paraphrase of that idea may be expressed as: "We, the Chileans, are leaving behind the third world, and supported by our successful economic model, are converging rapidly to European standards."

After democracy was restored in 1990, the new Chilean authorities did not change that perspective. During the participation of Chile in the ExpoSevilla,[101] developed in

101 The Universal Exposition of Seville (Expo '92) took place from Monday, April 20 to Monday, October 12, 1992 on La Cartuja, Seville, Spain. The theme for the Expo was "The Age of Discovery" and over 100 countries were represented. E. Garcia manager of Chilean Pavilion declare that "If we can transport an iceberg of 60 tons from Antarctica and install it in Spain, using a refrigeration system that let it support the Sevilla´s summer of 40° Celsius, we can transport with the same efficacy, Chilean fresh

Spain during 1992, Chile implemented a promotional stand built around a large piece of iceberg moved from the Chilean Antarctic Territory to Europe. The message was quite clear, "We are different. Chile is not a tropical country, but a "cold nation" very different from the rest of Latin America. With us, business can be done seriously". Underpinned by these concepts, the new Chilean economic authorities continued to promote trade openness and market liberalisation as key to the development of its economy and society. In this way, during the nineties, Chile became one of the most open economies worldwide, at the same time achieving one of the highest degrees of market liberalisation globally existent.[102]

Given this framework, it seems difficult to analyse the success or failure of the Chilean neoliberal model of development, without first dealing with the issues related to what should constitute its main outcome, the convergence of its economy with those of the developed world. In a second moment, it will be necessary to analyse if those successes and failures are related to new price systems induced by the trade openness or, on the contrary, by some institutional factors. For that reason, this chapter will firstly attempt to verify empirically whether GDP and the productivity of the Chilean economy have been effectively converging with more developed countries. However, to carry out this analysis, we will not use as a starting point the old neoliberal discourse that prevailed during the period of the dictatorship, but the new speech with which this was substituted, since 1990, by the new post-dictatorship Chilean authorities.

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products, like fruits or salmon, to any place in the world". Before ExpoSevilla was opened, The New York Times published an article in which it ironically described the Chilean idea of presenting the iceberg. The NYT said, "With a successful display at Expo '92, Chile seeks to show that it would be an ideal trading partner for the new European Community. But students of fiction can only smile when Chileans say that the project is also meant to prove that Chile is as much European as Latin American." («Chile's Chilly Idea» NYT, November 8, 1991).

102 In Chile, the first period of trade liberalisation began in 1976 and lasted until June 1979, a period in which 98% of pre-existing tariffs were reduced to a flat rate of 10% and almost all non-tariff barriers were eliminated. However, this process was reversed from 1982-1983 due to the severe economic crisis that affected the economy, raising tariffs to 20% in 1983 and 35% in 1983. In parallel, the exchange rate showed a strong devaluation from 1983-1984 followed by a period of incentives to export. Once this crisis was overcome, trade liberalisation was reinforced and gave rise to successive tariff reductions, from 35% in 1985 to an average of 11% in 1991. In 1999, there began a process of tariff reduction of 1% per year, up to 6% in 2003. From then onwards, the successive free trade agreement treaties signed by Chile led to an average tariff of less than 0.5% in 2010. A more detailed analysis of the various moments of Chilean economic openness may be consulted in Meller, 1994 and Ffrench-Davis, 2002.

We will emphasise in our analysis the relevance of discussions concerning the Chilean implementation of the new course of action, associated with the strategic proposals of the World Bank, the International Monetary Fund, the OECD and other multilateral financial organizations. Such proposals, after being accepted by the new Chilean authorities, promptly launched a new action programme which gave a fresh start to the old neoliberal model.

4.2. The Rise of the Washington Consensus

Our period of analysis (1990-2009) is clearly one in which new and powerful international forces were deployed worldwide. This situation had a profound impact on the evolution of the Chilean Model, in a way perhaps stronger than the influence exerted by other exogenous forces (like the role of the "neoliberal founding fathers" already referred to) in the initial stages of that model.

Towards the end of the 20th century, an important number of contradictions existing between the fundamentalist neoliberal discourse (Friedman, 1975, 1980, Hayek, 2001a, 2001b) and the practical results of their interventions became self-evident.

The recession induced by the neoliberal policies, that used monetary policies as a tool to slow down inflation, was unable to curb hyperinflation in the 1980s. The cutback in public expenditure, associated with a reduction or elimination of state subsidies for basic services and basic consumer goods, as well with a fall in public investment, had only ended up producing significant rises in levels of unemployment and informal labour markets. Although fiscal deficits financed with monetary emission had disappeared since 1976, towards the end of the 1980s, inflation had failed to lower numbers to less than two single-digits.

This situation was diagnosed by multilateral development organisations as resulting from the weaknesses of the neo-liberal monetarist approach promoted by Friedman and Stigler and consequently, since the beginning of the 1980s, a new proposal was developed by contemporary mainstream academics, and within multilateral organizations, by neoclassical economists positioned very close the boundaries of the neoliberal view.[103]

103 See: John Williamson's keynote address to the Congress of the Sri Lankan Association for the Advancement of Science, given while he was the Chief Economist for the South Asia Region of the World

The systematisation of these ideas in the late years of that decade, engendered a comprehensive theoretical framework, christened "The Washington Consensus". From this perspective, they proclaimed that inadequacy of neoliberal policies should be addressed through a range of policy interventions that conformed to a strategic programme, and which were systematised in the form of a Decalogue put in writing in 1989 by the English economist John Williamson (2004b). This list described a set of policy recommendations for Non-Developed Economies (NDE) and was promoted by multilateral financial organisations and the governments of larger developed countries (Williamson, 1990, 2004a). In fact, TWC constituted an action programme inspired by an intersection of common points between the radical neoclassical (or neoliberal) approach of the 1980s, and the moderate neoclassical approach of the 1990s, which exerted strong worldwide influence for almost two decades (Williamson, 1999). TWC´s Decalogue proposed that NDE should take action in the following policy areas:

1. Reduction or elimination of budget deficits.
2. Reduction and focalisation of public expenditure.
3. Tax reform that broadens the tax base and cut marginal tax rates.
4. Financial liberalisation, involving an ultimate objective of market-determined interest rates.
5. A unified exchange rate at a level sufficiently competitive to induce a rapid growth in non-traditional exports.
6. Quantitative trade restrictions to be rapidly replaced by tariffs, which would be progressively reduced until a uniform low rate in the range of 10 to 20 per cent was achieved.
7. Abolition of barriers impeding the entry of FDI (foreign direct investment).
8. Privatisation of state enterprises.
9. Abolition of regulations that impede the entry of new firms or restrict competition.
10. Provision of secure property rights, especially to the informal sector.[104]

Bank *(*Williamson, 1998).

104 In Chile, as in other countries of Latin America, the application of these recommendations was applied in a way highly biased to the old neoliberal prescriptions. "A unified exchange rate at a level sufficiently competitive to induce rapid growth in non-traditional exports", was only understood as a "unified rate", but not as a rate that promotes the exports of emerging enterprises. Abolition of regulations that impede the entry of new firms or restrict competition, were applied seriously only in cases in which larger enterprises looked for elimination of influence of public antitrust regulations, but not when new dynamic enterprise threatened incumbent large companies in any market. The provision of secure

A significant difference between TWC and the old neoliberal model was the increased emphasis given by the latter to macroeconomic reforms over microeconomic ones. However, this did not constitute an essential difference, but rather a change in emphasis. Despite the fact that neoclassical thought during half a century has maintained its leadership in the economic mainstream, towards the end of the Reagan government in the USA (1989) and following the resignation of Margaret Thatcher in the UK (1990), its more radical wing, the neoliberal approach, has lost much of its dynamism and influence in global public policies. Regarding neoliberalism, TWC represented a phenomenon that was in some ways analogous to the role played by "neoclassical synthesis"[105] regarding classical Keynesian thought. Nevertheless, contrary to "the synthesis", TWC did not imply the construction of a different model that had the same appearance. Instead, it suggested building a model that although still equipped with a distinct appearance, did not really exhibit major differences. In fact, even if the revisionism embodied in TWC implied a break with the more unrealistic and ideological aspects of the neoliberal model, within it the core neoliberal approach remained essentially unaltered.

In order to mark differences between the two models, some authors argue that TWC has never been identified with neoliberalism,[106] an approach, which they understood only as the ideas advocated by "The Mont Pelerin Society".[107] They have argued repeatedly that regardless of its well-known ten-point programme, TWC essentially advocated : 1) Macroeconomic Discipline, 2) Privatisation, 3) A Market Economy, and 4) Free Trade, but did not endorse monetarism, supply-side economics, low taxes, a minimalist state and free movements of capital.

However, given that the ten points of TWC´s policy and those four recommendations are both grounded in concepts that may be endorsed by the neoliberal matrix (Fine

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property rights, especially to the informal sector was never a topic taken seriously in Chile.

105 "The Neoclassical - Keynesian Synthesis" is a term coined by Paul Samuelson. It includes works that were developed from Hicks (1937) Modigliani (1944) and Patinkin (1948a, 194b)). In this synthesis the Keynesian approach, following the interpretation suggested by Hicks, included his Keynesian IS-LM diagram, which was supplemented by equations derived from the behaviour of maximizing agents typical of the neoclassical microeconomic scheme.

106 See: Williamson (2002) and his contributions to the compilation of Kuczynski and. Williamson (2003), pages 305-332.

107 See: *https://www.montpelerin.org/*

et al., 2001) and for that reason have been implemented in Chile for a long time, it is difficult to separate TWC suggestions from the points of the old neoliberal proposal.

As is generally acknowledged, monetarism was part of a specific contribution from the Chicago school to the neoliberal approach (Crouch, 2011), exerting a important influence on The Mont Pelerin Society through Milton Friedman. Essentially, he advocated for the maintenance of a constant money supply and leaving the economy to take care of itself. Because of this, monetarism re-oriented emerging neoliberal thinking from the issues of political philosophy or economic anthropology, which had historically been its major focus, to the area of macroeconomic policies (Lüders y Rosende, 2007:144-153; Hachette, 2007:35-49). In Chile, 1973-1983, the central points promoted by monetarism as tools of economic policy (Bardón et al, 1985) were:

1. Controlling inflation by keeping the monetary mass constant in relation to the growth of the GDP.
2. Using rising interest rates as an instrument of monetary restriction by encouraging savers to lend money to banks, thus facilitating credit for investment.
3. Maintaining high exchange rates by means of the restriction of money supply.
4. Any trade deficits must be financed with foreign debt (the monetary approach to the balance of payments).[108]
5. Maintenance of low wages so that investors have production costs that encourage them to undertake new projects which generate greater profitability.
6. Generation of a fiscal surplus with high taxes and low public expenditure that allows governments to keep liquidity to be used in times of crisis.
7. Privatisation of public services and state enterprises.
8. Trade openness and market liberalisation, with the aim of eliminating distortions (trade barriers and the discretional process of resources allocation) and pushing inefficient domestic producers out of the market.

The similarity of this programme with the TWC is substantial, and it can be asserted that, in Chile, the TWC constituted a sort of continuity of the neoliberal programme already underway. However, the first four points of this list are elements, which, despite their radical monetarist allegiance, were not at all essential to the Chilean model, or to neoliberal thinking, and for that reason were promptly discarded. In fact, after

108 In the Chilean case, an adjustment of the balance of payments was added via decreasing nominal wages and a fixed nominal exchange rate.

the banking crisis of 1982, the Chilean dictatorship introduced major changes in its initial approach, away from their original unrestricted defence of the first four points.

In 1982, Chile began a process of strong devaluation (18%) of the Chilean peso against the dollar. The Chilean Central Bank took control of the interest rate so that it was no longer determined by the market and introduced a rise in tariffs, which put to one side all attempts to use nominal wages as an adjustment variable of aggregate spending. (French-Davis, 1982).

If within TWC there was some kind of "abandonment" of main monetarist prescriptions, that situation, as the Chilean case shows, cannot be over-estimated in defining TWC as a proposal that left behind the neoliberal agenda. Abandoning monetarism as described by Foxley (1983), was a policy implemented during the dictatorship (1982-1985), driven by neoliberal economists (Buchi 2006, Lüders et al., 2012) who continue to defend that agenda. Following this line of reasoning, which understands the "abandonment of neoliberalism" as synonymous with the "abandonment of monetarism", presents several problems.

Firstly, in Chile, the neoliberal post-monetarist policies were practically identical to TWC proposals that would emerge a few years later, and they continued to be managed by neoliberal Chicago trained economists, who considered them to be continuing the neoliberal agenda. Secondly, it is not an easy task to sustain that TWC represented an abandonment of neoliberal model. In that case, we would also have to accept that the Pinochet economic reforms of 1982-1985 were the first Chilean attempt to leave behind the neoliberal model, an affirmation that, in Chile, neither neoliberal economists nor their opponents would be able to subscribe to.

In summary, it is sounder to assume that Chilean model did not lose its neoliberal character after monetarist abandonment; and that TWC proposals are almost identical to neoliberal´s non-monetarist ones and for that reason, can essentially be defined as a neoliberal policy program.

Essentially, since 1990, the dominant public policy in Chile has consisted of implementing ideas inspired by The Washington Consensus and extending them via the prominent influence of Chilean scholars trained in the design of public policies, mainly at US universities (Silva 2010). This group of professionals took into its hands the transition from the already modified neoliberal monetarist model into a new phase to be developed

under TWC recommendations. In our opinion, it is clear that changes in the functioning of the Chilean model implemented from 1982 were a pioneering approach to TWC ideas, rather than a rejection of neoliberalism. This first wave of corrections to "the model" represents a deviation from the monetarist approach that was more radical than the adoption of TWC approach several years later. Nevertheless, neither the conclusion of the monetarist phase of the model nor the adoption of the TWC proposals meant an abandonment of the key elements of the neoliberal model. However, the truly amazing event was that after the reestablishment of democracy at the beginning of the 1990s, the new Chilean governments assumed the implementation of TWC recommendations as their own programme.[109]

This adherence to the TWC mainly was expression of a unilateral subordination of the organisers of the anti-dictatorship and anti-neoliberal movement, to proposals of multilateral organizations that advocated for the consensus. It is true that Chilean centre-left leaders, once in power, adopted the essential elements of the model that they had previously fought, apparently under pressure of multilateral organisations. Nevertheless, there were also powerful domestic pressures in the same direction. Analysing the relationship between both influences, some authors states that, "*Many of the unpopular economic policies implemented by the Government of "La Concertación" obey less to the instances which have emerged from The Washington Consensus than to pressures from local economic powers in conjunction with multinational companies" (Larraín; 1999:3).*

According to other authors, local and multinational pressures would have resulted in a new way of evaluating the neoliberal model by the "anti-neoliberal" elite, under circumstances in which, as Castell (2005) describes, the determinant factors resulting from this decision are very hard to separate into endogenous and exogenous influences.[110]

109 When the Minister of Finances of the first democratic government, Alejandro Foxley, (Foxley, 1993) describes in detail the economic strategy of the first Chilean government (1990-1994) it is quite clear that this is a virtual paraphrase of the TWC Decalogue (see: Foxley, 1993, Pizarro, Kuczynsk*i* et al., 1995).

110 This phenomenon was repeated in all Latin America, involving both right and left wing governments and, of course, different forms of populist leaderships. However only in the Chilean case was there such a high level of conviction in the application of TWC prescriptions. As it is reported by Gilbert (2002), there were multiple cases in which the Chilean influence became very strong to the interior of multilateral organizations which, promoted instruments and policies previously designed and implemented in Chile, but not yet sufficiently matured in Washington D.C. A more extended analysis of this fascinating but important subject is unfortunately beyond the scope of this research.

The exogenous influences were not minor ones. As J. Williamson made explicit, in spite of its subsequent global application, the Consensus was developed as a set of specific recommendations oriented to exert influence on Latin American countries.[111] He stated: "*The first written usage was in my background paper for a conference that the Institute for International Economics convened in order to examine the extent to which the old ideas of development economics, that had governed Latin American economic policy since the 1950s, were being swept aside by the set of ideas that had long been accepted as appropriate within the OECD"* (Williamson, 2004b:1).

After this initial conference, emphasis was placed on the need to provide the Latin American economies with an economic orientation different from the one proposed by ECLAC and, at the same time, different from the most extreme aspects of the model implemented in Chile by the neoliberal. In this context, the new Chilean authorities assumed TWC as a very convenient policy option, politically speaking. At this point, the particularly weak first Chilean government post-dictatorship seemed to conclude that the possibility of a collision with the multilateral financial organizations was not a viable option.[112] Then, transforming needs to virtues in a very swift way, these recommendations began to be read by the post-dictatorship governments as part of a public policy design different from the neoliberal one. This means that, far from being regarded as a defeat, the new economic authorities assumed TWC recommendations as part of their own programme.

After 1990, the Chilean economic authorities adopted all TWC prescriptions into their administration, opening the capital markets as well as the real sector and implementing all the macro-institutional reforms advocated by the Consensus, assuming that they were implementing a non-Neoliberal development strategy.

The incongruity of TWC guidelines in Chile, as in the rest of the world, led at first to scepticism of some guidelines of the Consensus, and subsequently widespread

111 In the words of J. Williamson (2004a:199): *"The Washington Consensus was a product of its time, and so there was little recognition of institutional issues. Furthermore, the success of one Latin American country (Chile) that did a number of other things (such as pursuing countercyclical policies à la Keynes) that helped it avoid crises and mitigated the economic cycle, has pointed to some aspects of policy that did not receive proper recognition in 1989".*

112 It should be noted that, at the beginning of the 1990s, despite the collapse of the socialist countries, in the interior of the US Government and within multilateral agencies, the strategies of the cold war period continued to prevail and suspicions about the Latin American centre-left governments persisted.

discrediting of their strategies and policy prescriptions (Naim, 2000).[113] At a global level, during the mid-1990s and especially during the 1994-1995 Mexican peso crisis, the unassailability of Consensus policies began to be challenged. The unsatisfactory results in Latin America persisted, as in other emerging economies, following the Asian crisis. The new financial crises in Turkey (2000-2001) and Argentina (2001-2002) and the later financial crisis that led the world to a global recession in 2007 have seriously eroded the arguments of the remaining supporters of the Consensus (Gore, 2000; Soederberg, 2004). Thus, after more than ten years of painful adjustment to policies, the macro-economic equilibrium and the growth in productivity that would have justified the application of Consensus guidelines are almost nowhere to be found.

With its domestic focus, the Consensus ignored the challenges and consequences of globalisation, particularly in the financial sphere within which political, legal, cultural, and even geographical factors influence the financial system (Levine, 2005). Bank failures, balance-of-trade problems, and the financial crises that have shaken one country after another in the past twenty years have shown that merely liberalising markets, without effective institutions and regulatory frameworks, does not resolve the structural problems that exert influence over the process of transition from underdevelopment to development (Kingstone, 2006). As Rodrik (2006) says: "*The one thing that is generally agreed on about the consequences of these reforms (TWC) is that things have not quite worked out the way they were intended*".

In spite of this, the mixture of pressures coming from international agencies and the pragmatism of the new Chilean political elite, who tried to find new balances with the military and oligarchic establishment (e.g. Boeninger, 1997), resulted in a strong continuity of the essential elements of the neoliberal economic model through the prescriptions of TWC.

With the two first periods of the application of the Chilean Model (1973-1989 and 1990-2009), the country boasted nearly thirty-seven years of openness and liberalisation. It was expected that this strategy would lead to higher productivity and GDP per capita growth, increase competitive pressures on domestic producers, and expand greater

113 Criticism of the scarce or negative impact exerted by the Washington Consensus recommendations has obviously not been based on an analysis of the Chilean case. Especially when in the early twenty-first century, the failure of the political and economic transition of Eastern Europe - with the possible exception of Poland - as well as the Russian Federation, has been contrasted with the economic success of China and Vietnam, countries that have never adhered to the Consensus.

domestic access to international best practice technologies, production processes and positive externalities.

However, these expected benefits did not materialise, given that an appropriate institutional framework was not in place. Following TWC guidelines, the supporters of the Chilean model have emphasised that it was necessary, once the post dictatorship period had begun, to avoid the state adopting an activist stance to overcome market failures in critical areas, stating that the state must plays only a subsidiary role.

Chile has undertaken for the longest time worldwide each one of the recipes to influence the variables first outlined by neoliberals and then by TWC, stated as key to achieving convergence goals (Burke and Perry, 1998). However, if the country is not converging towards the levels of productivity and growth of the developed countries, at least has struggled to emulate them, but, despite the orthodoxy of Chilean economic policies, adopted neoliberal-neoclassical proposals would appear to be grounded on the wrong premise.

As a result, it is not clear if Chile would be genuinely converging on development. We will show throughout this chapter by using the Chilean experience as a case study that market liberalisation and trade openness do not seem to generate economic growth based on productivity if markets are not fully competitive and if a suitable institutional environment does not coexist with an adequate governance system.

4.3. What are we talking about when we talk about Convergence?

The convergence of NDE to the situation of DE (developed economies) is a goal shared not only by the elite but also by the great mass of people who live in these countries. Perhaps for this reason, in the field of applied economic research, few subjects have been reviewed as extensively as the convergence hypothesis advanced by Solow (1956, 1957) and later documented by Barro and Sala-i-Martin (1990, 1992, 2003a), Barro (1991), Mankiw et al. (1995) and by Ben-David (1996). The starting point for the convergence hypothesis is the existence of a link between the value of production and the level of use of factors of production.

Commentators expanded this assessment stating that this relationship can be approximated by an aggregate production function that presents diminishing returns to scale in both factors, but especially in capital. The existence of diminishing returns to scale in capital (or in the various types of capital considered in the neoclassical model) means that the product grows less proportionally to the capital stock. Thus, the marginal productivity of that factor would decrease.

With its build-up, a situation that is supposed to generate a trend of slowing growth rates over time. Given this factor, the concept of absolute convergence assumes that countries which are less developed and have less abundant capital would possess a higher marginal productivity. For this reason, it is assumed that poor countries should grow faster than wealthier ones.

According to this hypothesis, one can predict a non-conditional (absolute) convergence in per capita income from the poorest countries towards the levels of the more affluent.

This happens under the premise that the poorest countries would have a greater potential (ceteris paribus) for growth at rates higher than the richer countries (Solow, 1970). If capital and technology circulate freely among the different countries, that orthodox neoclassical growth model holds that international levels of income will converge in time.

The convergence debate has been extensively developed since the late 90s, but is particularly worth revisiting it in order to visualise the discussion in light of the Chilean case. Obviously, it would not be useful to try to reproduce the well-known exercises developed by Barro and Sala I Martin through which they try to demonstrate what kind of convergence predominates around the world.

Similarly, it would be redundant to replicate the already developed exercises looking to establish the mayor or minor influences of various parameters incorporated as conditional variables. Our interest is different and far simpler. We will only try to establish if incorporation of Chile to OECD[114] has been associated with the presence of a real convergence of the Chilean economy to countries of similar characteristics as the neoclassical and neoliberal theory hoped.[115]

114 Chile was accepted into OECD in 2010.

115 Incorporation to OECD requires all their members to demonstrate the -ex ante- presence of

For that reason, before we extract conclusions about "convergence", it is necessary firstly to conduct a short literature review in order to define which specific concept of convergence is most suitable to our purposes; secondly to establish if that kind of convergence was actually achieved, and thirdly to inquire about the meaning of the presence or absence of this form of convergence.

Then, our focus in this chapter will not be placed on the analysis of determinants of the convergence (or non-convergence) of the Chilean economy, rather in trying to clearly define if such convergence actually subsists, or otherwise, to what extent it existed.

4.4. The First Binomial of Convergence´s Meanings: Conditional or Unconditional?

When old neoclassical models started to become obsolete, Barro and Sala-i-Martin (1990) introduced mayor changes to the old views inspired by the Solow-Swan Model. They proposed two new key technical meanings of the word: "convergence". One is binomial: *conditional convergence and unconditional convergence* and the second is binomial: β *convergence and* ? *convergence*.

The first binomial refers to differences between two classes of convergence. The first one is "*unconditional (or absolute) convergence*", a process that occurs when the income gap between two countries decreases, irrespective of the countries' other characteristics (e.g., institutions, policies, technology, human capital, level and quality of investments, etc.), depending only on the initial endowment of productive factors and production per capita levels (Rodrik, 2011b).[116] This process of β absolute convergence may be expressed using the following model:

1. $$\Delta \log y_{i,t} = \alpha_i + \beta \log y_{i,t-1} + u_i$$

homogenous conditional conditions, and later to adhere to a set of policies defined as "best practices". TWC was strongly anchored in regard to the latter policies, and their prescriptions aimed to install a programme to produce conditional convergence. Based on this framework, TWC claims it is necessary to reinforce the characteristics that are usually associated to this conditionality. In their proposal, this would be compulsory for any NDE aspiring to overcome its underdeveloped status.

116 Rodrik (2011a) identifies the presence of this type of convergence affirming that there is indeed unconditional convergence (only) in individual manufacturing industries, but he cannot identify this kind of convergence at an aggregate level.

Where "$y_{i,t}$" is the GDP per capita of the economy **"i"** at time **"t"**; and **"α"** are the fixed effects, i.e., represents the persistent factors that retard the growth of GDP per capita.

The type of regressions used to test this model consider that there is convergence if the value of β is negative, assuming to $\beta \geq 0$ as a null hypothesis of no-convergence. Otherwise, the β coefficient allows us to identify the existence of convergence. If the coefficient is negative and statistically significant, that means that convergence must be accepted as verified. Generally, β absolute convergence refers to the approximation of GDP per capita or Average Productivity of Labour (APL),[117] measured across countries, regardless of their particularities.[118]

The models of exogenous growth, from Solow onwards, had insisted on the hypothesis of spontaneous absolute convergence. Nevertheless, soon that idea was abandoned within the neoclassical field, when a second concept named "conditional convergence" emerged. This new meaning of "convergence" refers to when the economic gap between two countries with similar characteristics becomes narrower over time. This is mainly because of the presence and influence of other features distinct from the initial level of GDP per capita. If all of these particular features are the same for an economy and they are grouped in a single vector ***X***, in terms of the growth-initial level regression as in equation (1) explained above, the sign of β must also be negative (Barro and Sala–I–Martin; 1991, 1992).

The new model may be expressed as:

1. $$logy_{l,t} = a_{ir} + \beta\, logy_{i,t-1} + \phi\, E_x i_t + u_i$$

Where **X** incorporates precisely the conditions formerly grouped with other variables that within the equation (1) were considered as equal and that are associated with each country **"i"** in a **"t"** moment of time, then ϕ will be the parameter that measures

117 APL is generally measured using the income per hour worked as a proxy variable.

118 Even knowing the weakness of the APL in capturing the real productivity of an economy, it is frequently used in place of a more accurate measurement such as the multi factor time-series. The use of TFP for international appraisals is very rare in the literature, given the difficulties of building a homogenous time series for several countries. Estimations of TFP requires complex adjustments (not always reproducible in a homogeneous way) to the quality of the factors, which would make it possible to form productivity estimations. Generally, there is no available and comparable data to facilitate this exercise.

the influence of these other explanatory variables (conditionality) on the dependent variable.[119]

According to this, to know if conditional convergence exists would require analysing only economies that share similar features and institutions, which can be expressed as a variable to be incorporated in the growth equation. In fact, when it is assumed that all countries converge to the same steady state point, the convergence is said to be absolute. In this case, it is obtained without considering the set of structural variables ***X,*** since it is assumed that it is more likely to encounter unconditional convergence in relatively homogeneous economies that do not differ significantly in their conditional variables.

These were the grounds of the concept of "conditional convergence". Theorists of this kind of convergence argue that NDE must install an institutional framework that promotes, at least, a strong presence of foreign direct investment plus trade openness and market liberalisation. This would foster technological learning processes, improve human capital and increase domestic productivity of capital. All these factors would enhance processes in which conditional convergence arises among countries with similar characteristics.

Those countries that lack such homogeneity should therefore aim at establishing internal conditions that allow them to obtain similar performance levels to those of the group of countries to which they want to converge. In fact, there are an important number of empirically observable correlations between the economic growth rate of countries granted by similar institutional frameworks, public policies and technological levels that are the attributes that vector X includes.

The new concept of conditionality refers instead to a process in which approximation of income per capita (or GDP per hours worked), observed across countries, depends on explicative-variables beyond GDP per capita of the base year. For instance, some types of institutions, policies, or the presence of initial conditions similar to those existing in the most successful economies of the rest of the world; exert an important influence (Acemoglu, 2009: 17).[120]

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119 As Islam (2003) assesses, the fact that β convergence be judged by the sign of β means that parameter β captures the partial correlation between the rate of growth and the level of income and also provides a measure of the speed of convergence (or divergence) of GDP, or income per capita growth, between countries or regions.

120 Several neoclassical authors have adhered to this analytical framework, arguing that in those NDE,

Throughout the period under analysis, the Chilean economy has been oriented in this direction, and for almost four decades Chile has been implementing development policies inspired by different versions of the neoclassical model, each having different levels of juxtaposition to the neoliberal approach, which acts as a general framework for all of them.

Looking at an extended period would enable us to define to what extent those policy options have made it possible for Chile to move forward, steering it towards a path of real development despite knowing that there is major evidence that the world is not evolving according to a growth path of "unconditional convergence". Instead, there is profuse evidence of "conditional convergence".

However, looking convergence process from another perspective, a second binomial exists which establishes differences between the other two categories: β convergence and ? convergence.

4.5. The Second Binomial of Convergence´s Meanings: β and s

Historically speaking, at the same time that theories of endogenous growth (Lucas, 1988; Rebelo, 1991) became known and began to gain credence, some authors like Barro and Sala-i-Martín (1991), tried to expand the conclusions outlined above by Solow, referring to the non-convergence of all countries to a single level of GDP per capita, but towards its own steady state.

From this point, the old neoclassical model was reconstructed, assuming that it may predict absolute β convergence but only in very specific contexts. This implied that absolute convergence would occur only if all countries have similar levels of technology, depreciation and population growth rates and only differ in their economic policies and initial capital endowment. In this event, it was agreed that the neoclassical model predicted that the growth rate of economies would be inversely related to the distance that separated the economy from its own steady state.[121]

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which exhibit a strong presence of foreign direct investment, it would boost technological learning processes. This in turn would improve human capital and increase the domestic productivity of capital, factors that would enhance processes of "conditional convergence" among countries with similar characteristics.

121 In that context, the expression "steady-state", although based on the concept coined by the classical

In the academic world, this conceptual leap was accepted as the logical evolution of the theory. However, in the political world, it was very difficult to explain to the layperson the transformation of the original promise of convergence with the developed world into a simple convergence with a theoretical steady state. It meant dismantling the bulk of the positive political influences, which the promise of convergence to developed countries level of live, exerted at the grassroots level.

Perhaps this is the reason why discussions regarding convergence, continued in the political world with little attention paid to the academic perspective. On these bases, the search for convergence factors went ahead with markedly different perspectives and focus.

Empirical studies focused on variables of human capital (Mankiw et al, 1992), qualitative variables that reflect the behaviour of the market and its regulation by the public sector (Gwartney, Lawson and Block, 1996), or the degree of corruption amongst others, trying to define the variables, which were responsible for an economy to achieve or not its own steady-state. Following this type of analysis, Barro (1991) estimated that more than 50 variables could be defined as conditional variables. Nevertheless, some of the most reputed neoclassical and neoliberal authors emphasised additional variables, including the mobility of short and long-term financial flow and the presence of restrictions on international trade (Sachs and Warner, 1997). It is precisely from here that they stress the importance of the implementation of certain macro-institutional reforms in Latin American countries.

These reforms were promoted by the neoliberal-neoclassical discourse as the most appropriate path to achieve a self-sustaining growth process, which would guide the region towards a path of economic convergence, providing it with characteristics similar to those of developed countries to which the continent aspired to converge. The available information (OECD, 2012b) belonged to OECD and non OCDE´s countries, shows that Chile present a situation a little less auspicious than the formerly described. In fact, the country has developed very weak catching-up processes, showing a productive gap with the USA almost unaltered between 1960 and 2009 (and even more so later).

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economists and the Solow-Swan model from the development of the NEGT in advance, took on a somewhat different meaning. It is estimated that the characterisation of the steady state of an economy is related to changes in conditions included in the ceteris paribus of the regression, which are able to assimilate any country to its most developed peers.

Chile has approached in this matter countries like Argentina and Mexico whose trajectory is clearly decreasing in the period under study. And surpassing only Brazil, a country whose trajectory is quite disappointing, after a period of recovery during the 80s. Therefore, comparing Chile with Korea (an OECD´s country) gives rather uninspiring results.

The main findings of convergence´s studies were that, once controlled in each economy, the particular determinants responsible for the GDP growth (in other words, differences associated to each steady state) could less problematically demonstrate the presence of economic convergence in large samples of countries or regions. A secondary finding was that speed of convergence in its "normal" level must be around 2% annually in order to generate conditional convergence (Barro, op. cit).

In order to refute criticism to their econometric analysis of cross section data that leads to the estimation of the coefficient β, the defenders of traditional neoclassical analysis supplemented it by evaluating the evolution through time using the standard deviation (**s**) of the distribution of income per capita. This means that there is **s** convergence if the dispersion of per capita income or output, measured as its square root of variance, diminishes over time.

Formally, **s** convergence is confirmed when the cross-sectional variance of the regional per capita incomes or outputs shows a statistically significant reduction between the initial and final periods of the sample. This new concept of convergence, introduced by Sala-i-Martin (1996), is associated with the reduction in the dispersion of a dependent variable (either GDP or any other) over time.

If GDP per capita values tend to be more huddled around the average as time passes, we would talk about **s** convergence. Then there is **s** convergence if the dispersion and inequalities between countries fall over time. The implicit idea is as follows: in the initial period, there is a high dispersion of per capita output due to the difference between rich and poor countries, which is expected to be lower at the end of the process of convergence toward the steady state. For σ convergence, it is necessary that there is β convergence and hence poor countries tend to grow more than the rich, but it is also necessary that the "other factors" do not act in the opposite direction.[122] Given

122 If the number of observations is very large, then the sample´s variance would approximate the population´s variance, in such a way that, as Sala-i-Martín shows, it would be possible to use equation: $Ln\ (yit) = to + (1 - \beta)\ Ln\ (yi, t-1) + \mu it$ in order to derive the evolution in time of σ^2_t. The condition that

that standard deviation which measures the dispersion of real per capita income or productivity over time is the square of variance**, s** convergence measures the dispersion of real GDP per capita or APL over time, based on the standard deviation of the logarithm of any or both variables across a group of countries or regions.

When the standard deviation tends to decline with the passage of time, such a result indicates that, in absolute terms, variances in GDP per capita or APL also decrease, a situation which is assumed as evidence of **s** convergence.[123]

Thus, all things being equal, we can assume that β convergence possibly leads to **s** convergence; where other things cannot be considered equal over time, then β convergence does not necessarily lead to s convergence, given that it does not necessarily imply a reduction in dispersion (Quah, 1993). This means that, instead of judging convergence indirectly through the sign of β**,** this should be judged directly by looking at the dynamics of dispersion of income level and/or growth rate across countries (Islam, 1998, 2000).[124]

In particular, Quah (1993a), showed that the presence of β convergence is consistent both with a constant distribution among economies as with increasing variance. Accordingly, in his view countries do not lead towards a conditional convergence but towards what Quah (1996) called the "Twin Peaks" model, or in simple words, a country's bipolarisation into two groups, a conclusion that some years before had been also obtained and advocated by Chatterji (1992) and Marcet (1994). Given this, it is necessary to define which measurement is pertinent to our research: Is it β**, s** or both?

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must be met so that this equation is stable is that $0 < \beta < 1$. If we do not assume that β is negative, there is β-convergence. Thus, if $\beta \leq 0$ we cannot have σ-convergence. From here, that β-convergence is a necessary condition for the existence of σ-convergence.

123 Barro and Sala-i-Martín (1991) measured this dispersion through the standard deviation of the logarithm of the product per capita.

124 In response to this point of view since the neoclassical theory, Sala-i-Martín argues that the two concepts of convergence understand the notion of β convergence as more relevant since it would measure the speed with which the GOP per capita has evolved and therefore its future projection, this being more important than the "current" situation (the level of dispersion). In his view, the degree of dispersion (or inequality) present in the event of high growth rates would be more relevant than the dispersion of the same.

Trying to prove whether Chile has achieved high rates of growth based on its low initial income is not the point that most interests us. It is plausible to assume that the neoclassical hypothesis of absolute convergence articulates in an appropriate form the fact that, in DE, GDP should grow less rapidly than in NDE. However, it would not prove that only initial GDP per capita is the determinant of growth or that it is the most relevant; nor would it prove that it should lead the country towards an unconditional convergence with the more developed countries.

Within the "absolute convergence" model, there are a significant number of non-modelled factors (ceteris paribus). These factors are associated with the variables that remain equal and play an important role in defining the product and productivity evolution. On the contrary, models of "conditional convergence" have been explicitly designed to test the influence of these kinds of variables in order to build well-calibrated equations of growth dynamics.

The option of identifying additional variables, which in the Chilean case would be partially correlate with the rate of economic growth, is not useful to our purposes. A long time ago, based on high quality variable identification exercises, the OECD identified specific types of institutional parameters that exert a strong influence on economic growth using "quality of institutions" as a country member's selection criteria. As reported by Sáez (2010), on the contrary to free trade agreements, the conditions of OECD membership cannot be quantified in terms of specific norms linked to foreign investment movements or import-exports flows. Nevertheless, the OECD defines what it calls "sound economic policies" that could lead to an increase in foreign investment, international trade and the growth of the economy. In spite of this, it is expected that given the restrictive conditions of countries' admission and their expected perseverance on these conditions, they move towards development and more specifically towards the OECD average income levels. This explains why, since 2010, Chile has decided to belong to the most significant Club of developed countries.

Within the OECD, there is a shared corporate approach, which has subsequently ensured that its members follow a specific approach to conditionality. This was not difficult for Chile, which implemented these measures before its entry into the OECD; a fact that Chilean's neoliberal advocates attributed to its pioneering policy proposals.

Nevertheless, there are no specific OECD guidelines referring to the fiscal or monetary policies of their members and none regarding the level of a country's external debt. Even

considering these points, Chile´s admission to OECD was in some way a guarantee of the presence of an important number of the more reputed characteristics, which the country shares with some of the more developed countries of the world. Given the presence of other explanatory variables in addition to the GDP of a base year, we could expect that the estimation of the R^2 of those regressions would indicate that the initial income explains only part of the growth of the GDP.

In the Chilean economy 1990-2009, there a lot of variables that presents a potential explanatory capability. These are linked to the abundance of mineral resources, the relative quality of human capital and the considerable amount of Foreign Direct Investment (FDI) very similar to Mexico and Brazil levels.[125] FDI is an important factor that would boost technological learning processes, improve human capital and increase the productivity of domestic factors and even the domestic level of investment capital. However, at this stage in the development of economic theory, there seems to be present a solid consensus as to which institutional factors are the most relevant in the explanation of economic performance (North, 1990; Acemoglu et al, 2005; Williamson 2007; Rodrik, 2011; Acemoglu and Robinson 2012).[126] On these grounds, the set of neoliberal-monetarist policies, as well as the policies of neoliberal orientation promoted by TWC, implemented a programme of institutional intervention in Chile aimed at stimulating endogenous growth conditions, essentially anchored in the new structure of relative prices induced by the liberalisation process.

Without making a radical break with the Neoliberal approach, the Chilean economic mainstream took the approach of conditional convergence, assuming the presence of some institutional variables within the Chilean model: solid property rights, freedom to contract and exchange, the presence of a State´s coercive capacity to enforce contracts between private parties etc.

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125 Chile has only 17 million inhabitants, Mexico almost 120 million and Brazil more that 200 million. The countries of the Latin American region, as an average, captures (in 2009) flows equivalent to 2% of each domestic GDP, but Chile stands out with an FDI-to-GDP ratio of 7.5% that year.

126 Acemoglu, Johnson, and Robinson (2001) develop the argument that differences in economic development are a result of differences in economic institutions rather than geographical factors or culture, using the different economic experiences of South Korea and North Korea to underpin their case. Using a stylised framework, they explain how economic institutions evolve endogenously and how they interact with political institutions. Supported by political institutions, economic institutions may be installed by small groups, which wield political power. As a result, economic institutions harmful to society but beneficial to these groups may be chosen, and societies may be stuck with these inefficient institutions because of commitment problems.

Given the incorporation of these institutional variables, neoliberalism assumed that the "success" of the Chilean economy was a good indication of how their own policies, which ensure conditionality, have contributed to the development of Chile and to its convergence with more advanced countries (Corbo 1985; Schmidt - Hebbel, 2006). Nevertheless, we have the impression that these statements are not necessarily in line with available evidence and in several cases, they mistake presence of a strong potential for achievements, with the identification of real tendencies.

Quah has shown that convergence only occurs in groups of countries in which certain characteristics of conditionality are shared in a very narrow way. Relevant convergence would be a sort of convergence club (Ben David, 1997), and so would not be the best method to seek convergence in large samples worldwide (like in: Sala-i-Martín, 1997),[127] on the contrary it should be tested in groups of countries where variable "X" (as Quah denominate it) is essential and relevant features are shared.

Given this, the course of action that we selected was first to test the presence of β convergence, as a *necessary condition* for the occurrence of convergence, within the OECD group that Chile joined, stressing that the *sufficient condition* (s convergence) is what is relevant to our purpose. Falsification of the neoliberal hypothesis does not require us to prove what will happen in the future with the convergence of the Chilean economy, but to prove if, after 35 years of economic opening, Chile has actually achieved an advance in the field of economic convergence.

Thus, our analysis is one developed after the implementation of openness and liberalisation policies, assuming consequences of neoliberal-monetarist policies implemented between 1973 and 1990, but focusing primarily on what occurred in the implementation of the neoliberal model from the year 1990 onwards. After that, in next chapters, we

127 Bernard and Durlauf (1996) demonstrate that cross-section tests are associated with a weaker notion of convergence than time series tests. They show how these alternative approaches make different assumptions as to whether the data is well characterised by a limiting distribution. As a result, they assess that choice of an appropriate testing framework depends on both the series of the specific null and alternative hypotheses under consideration, as well as on the initial conditions characterising the data being studied. Almost a decade later, Durlauf, Johnson, and Temple (2004), revisiting the econometric literature about the convergence hypothesis and the determinants of growth, discuss again the relative merits of cross-country analyses, time series approaches, methods and event studies that confirm presence of β convergence. They provide an extensive discussion of econometric issues, such as the presence of correlation of errors across countries. These authors stress that econometric findings about economic growth, should always be taken carefully because of limitations to the data and substantial model uncertainty.

analyse more carefully in which way institutional determinants of convergence are conditioned by trade openness or, in the contrary, they are core determinants of the opening outcomes.

4.6. The Chilean Case: An Empirical Test for the Presence of β and s Convergence

In order to develop the process of the falsification of the neoliberal hypothesis, we will use the available data to test both types of convergence. The findings of these processes should allow us to confirm whether the neoliberal hypothesis is plausible, and therefore if Chile has shown the process of convergence to developed countries because of its process of trade openness and the introduction of a neoliberal model of development. The best way to do this is to measure if there effectively exists a significant degree of β and-or s convergence of GDP and productivity in the Chilean economy, with the economies of member countries of the OECD.

Since Chile has been implementing an extended drive to assimilate it to the conditions that the OECD defined as desirable to stimulate convergence, it is possible to test the GDP and productivity convergence of Chile with OECD member countries from 1990 to 2009, from even long before Chile joined this select club (2010). Chile is the only country in this group that was not a member of the OECD in 1990, although it had been applying policies consistent with the proposals of this organisation since at least fifteen years prior.

For this reason, its inclusion is valid. Then, rather than regress to an equation of conditional convergence in order to assess the weight on the growth of the multiples variables associated to OECD´s conditionality, we will assume that, to a greater or lesser extent, the prerequisites for admission to the OECD ensure a condition common to the 25 countries surveyed.

Therefore, we will firstly test if there is a negative relationship between initial income and growth. If that condition is proved, variance of GDP and APL (Average Productivity of Labour) data will be analysed in order to visualise if there exists convergence of those OECD countries (including Chile), around the arithmetic mean of both variables of analysis: product and productivity. Based on our findings, we will evaluate the specific

behaviour of the Chilean economy in relation to the general trend observable in the group under consideration.

For this purpose, we will use time series data provided by the OECD (2013) about real GDP per capita (at PPP) and APL (measured as GDP per hour worked) for the period 1990–2009. The GDP and APL series incorporates homogeneous data, from 1989 onwards, for Chile and the other 24 countries that were OECD members in 1990.[128]

The GDP per capita PPP in USD of 2005 includes homogeneous estimations made by OECD and the productivity series includes homogeneous estimations of GDP per hour worked, a measure of Average Productivity of Labour, also estimated by OECD. The formula used for estimation of average GDP per capita growth rate for each country **(i)** throughout this period is:

$$(1)\boldsymbol{GDPGrowthRate} = \boldsymbol{LN}\sum_{t=1}^{n}(\boldsymbol{Yt}+\cdots+\boldsymbol{Yn})\boldsymbol{i}\text{-}\boldsymbol{LN}\sum_{n=1}^{n}(\boldsymbol{Yt}\text{-}1+\cdots+\boldsymbol{Yn}\text{-}1)\,\boldsymbol{i}$$

Where Y is the GDP per capita of each year "***t***", of each country "**i**", measured by the OECD at PPP and expressed in USD of 2005

Y_1, until Y_n is the GDP per capita of destination years (1990–2009)
Y_{i-1}, until Y_{n-1} is the GDP per capita of the preceding year (1989–2008).

The formula used for the estimation of APL growth rate for each country **(i)** throughout this period is:

$$(2)\boldsymbol{APLGrowthRate} = \boldsymbol{LN}\sum_{n=1}^{n}(\boldsymbol{Zt}+\cdots+\boldsymbol{Zn})\boldsymbol{i}\text{-}\boldsymbol{LN}\sum_{n=1}^{n}(\boldsymbol{Zt}\text{-}1+\cdots+\boldsymbol{Zn}\text{-}1)\,\boldsymbol{i}$$

Where Z is the GDP by hours worked each year (APL), measured by the OECD at PPP, of each year "***t***", of each country "**i**", and expressed in USD of 2005.[129]

128 Henceforth, we will refer to these 25 countries only as OECD countries.

129 GDP per hour worked is a measure of factorial productivity. It measures how efficiently labour inputs

Z_1, until Z_n is the APL of destination years (1990–2009)
$Z_{i-1,}$ until Z_{n-1} is the APL of the preceding year (1989–2008).

Data obtained by applying these formulas is shown in Table 4.1 below.
In this table, the natural logarithms of GDP PPP Growth Rates were calculated for the period 1990 to 2009 with the above-mentioned formula (1). They are presented in the first column.[130]
The natural logarithms of APL were calculated for the period 1990 up to 2009 with the above-mentioned formula (2); results are presented in the first second column.

The natural logarithms of GDP per capita PPP of base year 1989 were calculated for the period 1990 up to 2009 and are presented in the third column.

Table 4.1. Linear GDP PER CAPITA and Average Labour Productivity OECD Member Countries

Country	Ln GDPpp PPP Growth Rates 1990–2009 (US$ 2005)	Ln APL Growth Rates 1990–2009 (US$ 2005)	Ln GDPpc PPP base year 1989 (US$ 2005)
Australia	0,017941	0,016814	10,13459
Austria	0,016723	0,014888	10,10906
Belgium	0,013765	0,013275	10,10234
Canada	0,01151z4	0,012312	10,21816
Chile	0,034423	0,032765	8,79844
Denmark	0,011437	0,013213	10,12996
Finland	0,013920	0,021089	10,04875

are combined with other factors of production and used in the production process. OECD defines labour input as total hours worked of all persons engaged in production. That Average Labour Productivity (APL) only partially reflects the productivity of labour in terms of the personal capacities of workers or the intensity of their effort. Given that countries of lowest level of GDP per capita are characterised by the low productivity of their most abundant factor of production (labour), we would expect these countries' development path of APL to be negatively correlated to the initial level of GDP per capita.

130 It can be argued that there may be some limitations to the model used in the present study for calculating path of growth rates in relation to base year, but the findings of the present study are in line with earlier studies made in this area (Barro and Sala-i-Martin, 1992; Barro, 1996, and Acemoglu, 2009). Whilst these authors used other models for calculating the growth rates of GDP, the same findings can also be reached by using the present mode. It is similar to the GDP estimation technique proposed by Kumar for the Indian case, which is simple and does not require any advanced mathematical tools or software for calculating the growth rates of GDP per capita (Kumar, 2011).

Table 4.1. Continued.

Country	Ln GDPpp PPP Growth Rates 1990–2009 (US$ 2005)	Ln APL Growth Rates 1990–2009 (US$ 2005)	Ln GDPpc PPP base year 1989 (US$ 2005)
France	0,009993	0,015204	10,07872
Germany	0,012492	0,015830	10,11961
Greece	0,019782	0,014520	9,74939
Iceland	0,014437	0,024340	10,14808
Ireland	0,031843	0,030496	9,75460
Italy	0,006486	0,006793	10,05571
Japan	0,007714	0,017377	10,13421
Luxembourg	0,023530	0,011210	10,62148
Netherlands	0,017526	0,011355	10,14250
New Zealand	0,013580	0,011409	9,86867
Norway	0,018383	0,016819	10,36907
Portugal	0,015089	0,014687	9,64762
Spain	0,016857	0,007898	9,85245
Sweden	0,013795	0,018099	10,10687
Switzerland	0,006960	0,009974	10,40915
Turkey	0,022008	0,024420	8,90485
United Kingdom	0,016340	0,018453	10,05351
United States	0,012931	0,018828	10,36092

Source: Data for Chile and others 24 countries members of OECD since 1989 and before: APL is estimated as GDP per hour Worked.

The equations used to estimate a regression model of cross-section data for the 25 OECD member countries, are reported below.[131][132]

$$(3) \quad \Delta \mathbf{GDP}_{i,t} = \alpha + \beta \mathbf{LN}(\mathbf{GDP}_{i0}) + \varepsilon_i \qquad \text{(Model 1)}$$

$$(3) \quad \Delta \mathbf{APL}_{i,t} = \alpha + \beta \mathbf{LN}(\mathbf{APL}_{i0}) + \varepsilon_i \qquad \text{(Model 2)}$$

131 All references to GDP refer to GDP per capita.

132 In the literature, the first regression with real data in order to measure the real convergence between the two economies was performed by Baumol (1986), and then the equation utilised here is the proposed by Baumol but slightly modified in order to incorporate the GDP growth measurement proposed by Kumar (op cit).

Where: Δ is the growth rate of each variable estimated using equation (1) and (2). Additionally, each country is denoted by the term **i**, which ranges between 1 and 24; α is a constant level, β is a slope parameter, ε is a random component and **0** and **t** are numbers index indicating the time (e.g. each year between 1990 and the year 2009). Base year 1989 is identified with the subscript **0** and **T** is the number of years of the sample (20). Parameters of the linear regression model of cross-section data are estimated using least-squares method (OLS). The model was verified statistically at 5% significance level and for the calculations; the Stata program will be used. Regressions were subjected to statistical and econometric verification, which includes tests of autocorrelation, heteroscedasticity, normality and randomness of explanatory variable. Autocorrelation was tested using the Durbin-Watson (D-W) test and graphically using the autocorrelation (ACF) and partial autocorrelation function (PACF),[133] at a level of 5% of statistical significance, a normal distribution of residuals can be observed, and then the model can be considered without autocorrelation. When we plot regression of both growth rates (LN GDP per capita PP) $_{1990\_2009}$ and (LN APL) $_{1990-2009}$ (model 1 and model 2), against initial (GDP per capita) $_{1989,}$ we can see in Figures 4.4. A and B that the linear GDP per capita and APL´s growth rates of the sample, fits convincingly with forecasts of neoclassical theory. However, several particular situations problematize this framework.

133 Additionally, Heteroscedasticity was tested using the White´s Heteroscedasticity Test, in such way a way in which the model can be considered Homoscedastic. Residuals normality was tested using Jarque-Bera test, finding a normal distribution of residuals. Randomness of explanatory variable was tested using t-test, and on the selected level of significance, explanatory variable can be considered as random. Subsequently, this econometric model was verified economically and its results interpreted.

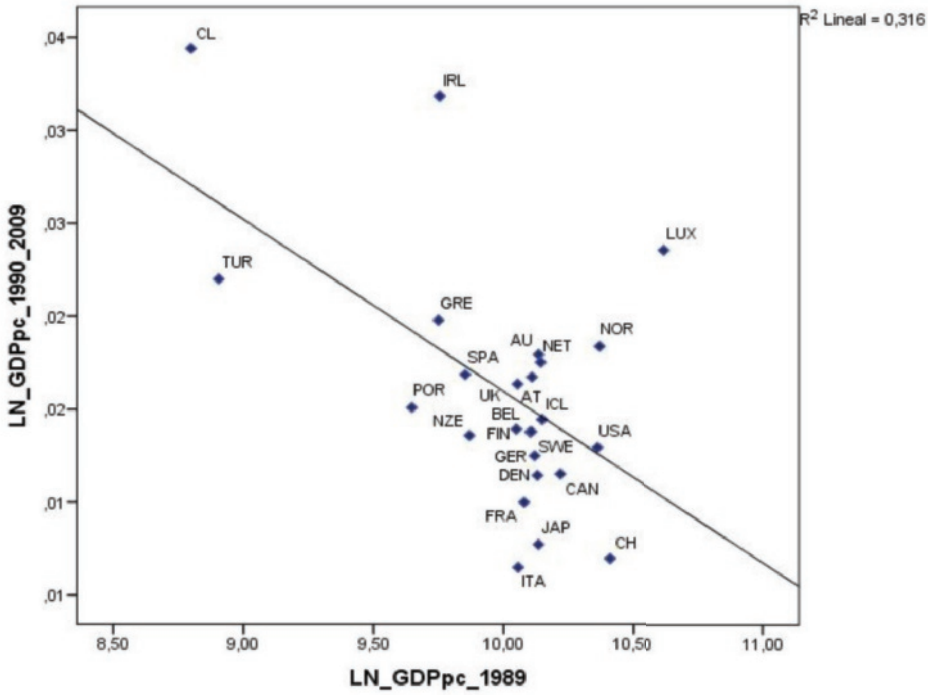

Figure 4.4 A. Convergence of GDP pc: OECD 1990-2009

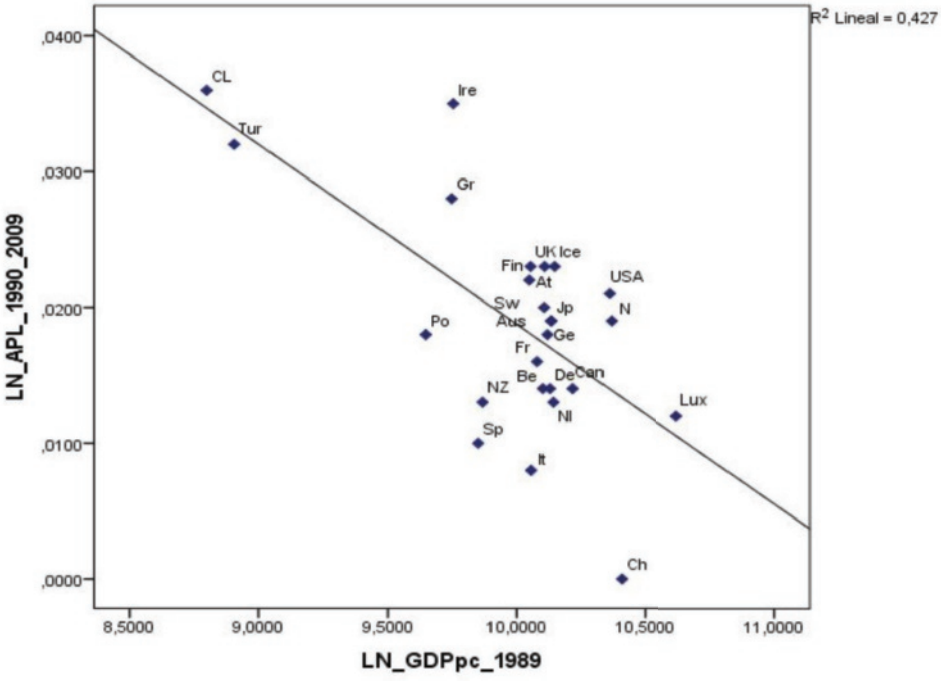

Figure 4.4 B. Convergence of APL: OECD 1990-2009

4.7. What do Regressions of Incomes and Productivity Show?

In Figures 4.4. A and 4.4 B above, it is clear that regression between the initial GDP (1989) and GDP per capita and APL growths rates[134] in general show the negative sign of a relationship between both dependent variables and the independent one. This performance fits with neoclassical theory

	(1)	(2)
Variables	AVRG Growth 1990-2009	APL 1990-2009
GDP 1989 *	-0,117	-0,00892
	(0,0026)	(0,00288)
Constant *	0,132	0,106
	(0,00259)	(0,0288)
Observations	24	24
R-Squared	0.479	0,303

Chart 4.1. Standard error in parentheses
* p <. 0,01

Square regression coefficients R^2 are -0.479 in the first regression and -0.303 in the second one. This shows that GDP per capita of the base year explains those percentages of dependent variables GDP per capita and APL 1990-2009, a result acceptable given the simplicity of the equations used and the inclusion of multiple variables. Our findings are consistent with presence of β conditional convergence as described by Barro y Sala-i-Martín, but also with Quah's proposal (1997) about the presence of convergence clubs formed endogenously and characterised by the presence of different dynamics of convergence, depending more from the institutional characteristics of the countries than the initial distribution of incomes.

All the OECD member countries since 1990 were included at the sample, except Luxemburg.[135] Exclusion of Luxemburg is easily understood. Luxembourg is a country,

134 The estimates of labour productivity used here are mainly based on data obtained from OECD Annual National Accounts (2010). A Rising Labour Productivity growth means the presence of higher levels of output for every hour worked. The OECD series of Multifactor Productivity was not used for the core analysis given that they are discontinued and are not available for all OECD member countries of our sample.

135 Luxembourg's tiny high-income economy features moderate growth, low inflation, and low

which clearly starts from a higher level of GDP than the rest of the OECD member's countries and, given the particularities of this small economy, has maintained higher output growth rates. However, these high growth dynamics in a country with greater initial GDP is only due to the extreme peculiarity of the Luxembourg economy.

Within the variables that are assumed constant, the savings rate plays an essential role in the growth, making possible the presence of substantial capital currents flowing towards Luxembourg´s banking sector. This situation has allowed this tiny country to generate large increases in GDP per capita and to finance the expansion of the real sector of the economy through low-cost financing. The characteristics of Luxembourg's financial sector are not precisely those recommended by OECD, or by Basel II, but based on this distance from OECD policies during the analysed period, Luxemburg permitted the influx of important shore financial flows seeking the benefits of a tax haven.

This specificity makes it extremely difficult for other countries to reach similar levels of financing for their development as Luxembourg, and thus effectively converging at their high level of GDP per capita over time.

The negative β coefficients in both regressions (-0.0117 and -0.0089), must be associated with the presence of a clear negative relationship between linear GDP per capita and APL growths and the linear GDP per capita of the base year. Given these results, the presence of β convergence of GDP per capita and APL of the OECD members countries included in the sample, cannot be rejected. However, remains in doubt if

unemployment. Their industrial sector, was dominated until the 1960s by steel, but nowadays has been diversified to include chemicals, rubber, and other products. During the past decades, growth in the financial sector has been more than compensated by the decline in the steel sector. Services, especially banking and other financial exports, account for the majority of economic output. Luxembourg is the world's second largest investment fund centre, the most important private banking centre in the Euro zone and Europe's leading centre for reinsurance companies. There important concerns about Luxembourg's banking secrecy laws, and its reputation as a tax haven, led in April 2009 to it being added to a "grey list" of nations with questionable banking arrangements by the G20. Luxembourg adopted some months later (in a way that is not reflected in our data) the OECD standards on exchange of information and moved into the OECD category of "Jurisdictions". The particular characteristics of the Luxembourgian economy do not enable it to conform so easily to the context in which the other OECD economies operate. In this light, we could say that, in that exclusive club composed mainly of big rich economies, this tiny and very rich country possesses a very different institutional context than all the others OECD countries. Its GDP presents a more erratic performance within this period, with a substantial standard deviation, meaning that its GDP has important deviation, each year, in relation to the average national GDP of that period.

the speed of the convergence is appropriate and whether it is reasonable to expect the next 87 years the OECD and Chile maintain its growth rates of productivity and GDP, an indispensable condition to make convergence possible.

In our case the coefficient R^2 of the first regression, which we are correlating to our independent variable (GDP per capita 1990-2009), suggests that just one explanatory variable (GDP per capita of the base year) explains 0.48 of the variance. In the second regression when we are correlating the second variable (APL 1990-2009) with the GDP per capita of 1989, R^2 suggest that APL explains 0.30 of the variance. Thus, R^2 shows, in both cases, an adequate explanatory capacity of the variations in the dependent variable attributable to the independent one suggesting that APL is a very important factor in determining the evolution of the GDP. The convergence β coefficients shows not only an inverse relationship between the country initial GDP and its future rate of GDP and APL growth. It also shows, in the course of the analysed period; that the OECD countries in our sample tend, to converge at an annual average speed of convergence close to Barro's speed estimations of 2 - 5%.[136] However this trend is heavily influenced by the high rates of the golden period. Is not clear if tendency would remain constant if the average growth of GDP and APL were the recorded among 2000-2009 and clearly the conclusions would change drastically if in our estimations were included the decreasing rates registered during the period 2000-2016.

Given the linearity of the selected model we are not only interested in the sign of the parameter β but also the speed of convergence of the GDP per capita, which defines the period necessary to make economies exceed half the distance that separates them from their steady-state. That means that at a speed of 1.2%%, it would take 60 years to eliminate half of the initial OECD´s GDP gap.

If, instead of focusing our attention on the trend or close the GDP gap among the OECD´s country members, then we focus our analysis on estimating the potential speed of closing of the gap between the Chilean GDP and the OECD average GDP, results would depend on the assumptions used.

In the course of period 1990-2009, Chilean GDP per capita grew at rates of 5% annually; in contrast, OECD GDP in average grew only at the 1.64 % each year. If

136 Speed of convergence could be defined as $\lambda = 1/T \, LN \, (1 + \beta i \, T)$, were T is the length of analysed period of time. Conversely the period of time that would, for example, take the economy on closing half of its GDP gap, can be estimated as: $t = LN \, (0.5)/ \lambda$

these rates remain constant, convergence (equalisation) between the Chilean GDP per capita and the OECD GDP per capita would be obtained in the year 2028, in which Chile would record a level of USD 44.412 per capita and the OECD USD 44.056.

However, the growth rates of both have fallen sharply and both OECD and Chile are facing major economic crises. Currently (2016), Chile's rate of GDP growth is projected at around 2% per year and the OECD around 1% a year. Maintaining unaltered this trend, the convergence to a unique level GDP per capita would be towards the end of the 21st century, with 2097 being the year in which Chile would exhibit a GDP per capita $79.142, slightly superior to OECD average of 77.635 USD.

In the short term, this trend towards convergence is extremely weak and the trend of the GDP evolution does not seem to be able to sustain itself in you time due to the weak development of productivity. This weak support of productivity not only is observed visualising the formerly described average productivity of labour.

The information available on multifactor productivity in the Chilean economy, as displayed in Figure 4.5. shows that when considering information about period 1960-2009, under 0.42% and twenty years (1990-2009) under 1.34% on average and are not observed conditions that allow to suppose that this situation will change substantially in the coming years. On the contrary, the TFP has been worsening from 2009 onwards.

The antecedents are unequivocal in realizing that productivity represents a front of great vulnerabilities in the Chilean economy (OECD, 2018). Instead of contributing each year to the growth of national income, it is currently deteriorating. The Chilean economy, by lowering its productivity, has stopped advancing along the path of convergence, just as it had done during its golden decade.

The available information (Central Bank, 2018) shows that an important source of loss of efficiency in the Chilean economy is the mining sector, whose TFP fell, on average, by over 8% per year between 2002 and 2009. Given the importance of mining in aggregate GDP, this phenomenon has been mentioned (OECD, op. cit.) as a risk factor for long-term growth.

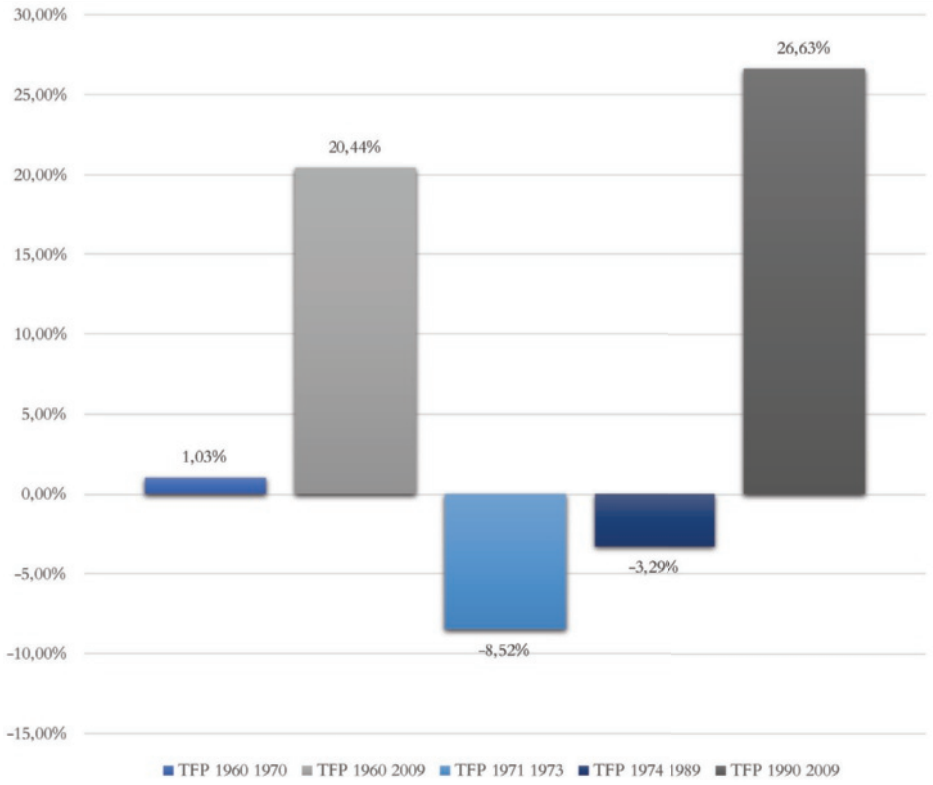

Figure 4.5. Evolution of Total Factor Productivity. Chile, 1960-2009.
Source: Author´s elaboration on data of Ministry of Finances, INE and Central Bank (1960-2009).

in Chile, the multifactorial productivity (TFP) completed half a century (1960-2009) growing.

The remaining sectors play in the economy a less critical role than the mining sector, but exhibiting, since the end of the last century, a clear tendency towards stagnation that has been compensated only by the effect (in the 1990-2009 average), of the virtuous effects of the golden cycle of growth that culminated in 1997.

4.7. Economic Convergence and Institutional Environment

One of the most important outcomes predicted by supporters of the Chilean model of development was the convergence of the country´s GDP to that of developed countries. Neoliberal theorists promoted the idea both of these processes would be

powerful devices that would allow the Chilean economy to increase growth and productivity, displaying an inclusive growth process, supported by trade openness and market liberalisation". But, when the real-world effectiveness of the core promise of the neoliberal model of development is subjected to empirical proof of its truthfulness, this undertaking does not seem to be fulfilled.

The figures formerly reported warrant that a model of development such as the Chilean one, which promised a convergence towards development using as a tool a drastic process of neoliberal reforms, is in a condition to only offer weak progress after almost 40 years of trade openness and liberalisation. The country will require almost another century to realise its projected outcome, making this an unattractive promise. Its lack of appeal rests, in this context, on the uncertain validity of the neoliberal proposals associated with the convergence of the Chilean economy.[137]

The actual relationship existing between the initial level of GDP and ulterior GDP growth in countries like Chile do not fit neoclassical theory. Chile, the country with the lowest GDP per capita in 1990, (U$ 6,624 in 1989), is the country that obtains a higher GDP per capita growth rate. Nevertheless, Turkey the second lowest income country (after Chile), does not obtain a similar performance. However, Ireland, initially a high-income level country; achieved impressive GDP growth rates and present performances in disagreement with the theory.

If in the end, the economic opening aims to generate the conditions so that, any economy that opens its borders may be placed in conditions to enhance productivity and a technological catch-up process (measured as the quotient between the labour productivity of each country and the USA), the success in that process should lead to a solid growth of the GDP that allows that economy close its productivity gap with the most advanced economies. Unfortunately, this does not seem to be the case in Chile, since in its economy the level of growth that could bridge the gaps in any measure was limited to only a decade, and is characterized by conditions of difficult reproduction.

Not all of these OECD member countries define GDP evolution in function only from its initial GDP level. The fact that all the other things tend to be equal, has a very

137 This optimistic scenario can already be rejected; between 2009 and 2014 the rate of growth of GDP per capita PPP of Chile was just 2.6 %, far from the expected 5%. From 2014 to 2016 the average was 1.94%. Onwards prospects are determined by the stage of international economics, not allowing Chile to be too optimistic about growth.

important effect given that ceteris paribus conditions imply homogenous policies and a similar institutional context. In spite of the general influence of a similar institutional context in which these countries evolved, in some national cases that context looks less homogenous than one may expect.

In OECD´s countries the policy´s dissimilarity produces clear behavioural variances between countries, a situation that seems to prove the presence of β conditional convergence. However, we can differentiate three countries that had economic policies that were atypical of OECD in some aspects.

In 1989, Turkey had a GDP of US $ 7,368.[138] Nevertheless Turkey did not belong, in the analysed period, within the OECD of countries with higher growth in their GDP per capita. One possible explanation is that Turkey has been reluctant to apply all OECD prescriptions.

During 1990–2009, its economy was not fully open, its public sector was not heavily privatised and its monetary policy has only slowly been approaching OECD practices.

Given this, it is possible to explain the low level of Turkish income growth throughout the analysed period from a neoclassical perspective, by their relative distance from the path of economic reforms recommended by OECD.[139] Meanwhile, said disengagement with the OECD´s cross-compliance conditions may explain their lower rates of growth. The case of Ireland is similar. During 20 years, the Republic of Ireland experienced a great level of economic growth, evolving from an agricultural economy to a non-agricultural one. In less than a decade, Irish GDP per capita overtook the economies of Germany, France, Japan and the average of the fifteen European Union (EU)

138 By the end of 2009, Chile had already achieved a GDP per capita of $13,855, surpassing Turkey, which only achieved a GDP per capita of $11,622 that year. However, despite its positive performance, Chile is fairly far from converging with the income levels of the selected OECD member's countries, whose average GDP per capita in 2009 was USD 32,342 with the median being $32,298.

139 In Turkey during 1990 to 2009, inequality increase and poverty has been maintained, in figures that include over the 30% of the population. The country has also exhibited the largest productivity gap between modern high-tech firms and small and informal companies within OECD economies. The OECD has been promoting flexibility in Turkish labour laws, making labour markets more flexible. Also, it has been promoting structural changes to the Turkish economy that allow to it attract direct foreign investment that finances its current account deficit without creating risky external debt. As we can see, this national policy is not closely aligned to policies implemented by the others OECD countries.

countries, exceeding those of these major industrialised and developed nations by more than 20% (Murphy, 2000; Whelan, 2013).

This growth was due to a strategy of FDI attraction. Multinationals like Oracle, Lotus, IBM, Intel and Microsoft established major operations in Ireland making it the largest exporter of software in the world at the end of the nineties, and one of the largest exporters of pharmaceutical products. Investment in human capital and in research and development was also significant.

This situation mobilised substantial amounts of foreign savings to Ireland and surely constituted an important cause of their fast growth. Ireland was a "good student" and their performance was aligned with theoretical expectations. Nevertheless, in the case of Turkey, there are many doubts about whether they are in condition to be homologated to the others OECD countries, and as to whether their "conditionality" is comparable to existent in others OECD countries.

In the Chilean case, throughout this period, the country exhibited linear average GDP per capita growth rates higher than the other 24 OECD member's countries. This fact, at a superficial glance, seems to confirm the neoclassical hypothesis of conditional convergence. However, the presence of regression´s negative sign does not imply that low Chilean income in 1989 is the reason why the country grew faster than the high incomes countries, when the other characteristics are controlled.

A by-product of the neoclassical assessment about this issue is that a rich country can grow faster than a poor country if the distance from its own steady state is further, or if it possesses certain characteristics in the remaining variables that explain this speed.

In that case, each country would possess its own conditional convergence logic, which would depend more on the relationship between introduced and independent variables in the growth equation, than on the variables included in the "ceteris paribus" condition of the same.

The above regression results seem to confirm this corollary and thus the neoclassical conditional β convergence hypothesis. When regression is run using APL data fit in a very similar way to the GDP per capita case ($R^2 = 0.303$), the four countries of lower initial GDP per capita were Chile, Turkey, Portugal and Greece (from least to greatest). Nevertheless, the higher productivity´s growth between 1990 and 2009 corresponds

to Chile, Ireland, Turkey, Iceland and Finland (from greatest to least). In sum, even though Chilean performance once again looks as if it fits within the neoclassical framework, it is not easy to explain the presence of higher productivities in some of the other countries. This is especially true if they present a negative relationship between average labour productivity and initial level of GDP, at least if we only try to explain that performance based on initial level of GDP per capita.

All OECD countries, with the exception of Chile and Turkey, are rich countries with high average labour productivity. The direction of productivity changes in those two countries is not well predicted by the absolute convergence hypothesis. In the Chilean case, APL in 1990 was only USD 8.9 per hour worked. In 2009, after growing 96%, it was USD 17.4 per hour. Turkey whose APL was USD 13.2 in 1990, in 2009 exhibited an APL of USD 21.6, growing 64%. This means that both countries developed their APL significantly in relation to the growth of the OECD country average (38%). Nevertheless, in 2009 Chilean APL continued to be 85% of Turkish APL, and 52% of OECD countries' productivity average.

In both countries, there are segments (mostly LSE) that in almost all productive sectors showed impressive productivity rates. Nevertheless, often far larger segments of firms (mostly MSME) continue to have low productivity rates. Both countries need to improve productivity. However, Chilean companies should deal with this context using near-zero tariffs, whilst the Turkish firms did it with indirect tariffs and import-related costs, which drove prices up by as much as 38% (Adam & Moutos, 2008).
The Turkish economy features a process of gradual trade openness and liberalisation that is less radical than Chile. However, one of the remaining barriers to productivity in the sector has been the series of sharp macroeconomic contractions and expansions in the 1990s; the oscillation has caused dramatic domestic demand swings and in turn has resulted in relatively low capacity utilisation. Turkey, from 1990 to 2009, was quite distant from the terms recommended by the OECD and presented a mediocre performance of GDP. It seems to soundly fit that hypothesis that, given the different institutional frameworks of Turkey and Chile, Turkish productivity must grow less than Chilean. If both countries have access to the same technologies, their differences can only be explained by differences in their particular institutional economic frameworks, which orient them to their steady state.

In the cases of Iceland and Finland, both economies have been oriented towards a new specialisation pattern based on high tech production activities, into the frame of

a long-term industrial policy that has had a main role in their successes (Barry, 2002; Berghäll and Kiander, 2003). However, in the case of Iceland (at the fourth level of APL), productivity remains stagnant from 1990 to 2000, then increased significantly from 2000 to 2005 and after that did not change much from 2006 to 2009.[140]

In sum, given the context described above, our regression´s results seem to confirm the presence of β conditional convergence of APL, even if we still cannot disprove the null hypothesis that Chile and OECD do not exhibit σ convergence over the period under analysis. We will therefore perform new analyses in order to confirm the possible presence of σ APL´s convergence.

Despite this, currently the neoclassical conclusions formulated by Sala-i-Martin (2003:139) fully agree with our findings. They indicate, in the same way that in the case of GDP per capita, which there is not a countrywide convergence to a unique position of APL. Quite to the contrary, rich countries (such as Luxembourg) may become even more productive than poor countries such as Turkey, whose GDP is climbing less than their productivity.

Given that, the most important point concerning the evolution of distribution of all the countries is to stress that each steady state depends essentially upon institutional variables (assumed as constant in our equation). If those variables depend upon national institutions, then the influence of such "other factors" on variance of GDP and APL should be measured with the sigma parameter. Convergence and divergence should then be calculated as the standard deviation of the sample, and this should be defined as the presence of some kind of dispersion of GDP per capita and APL overtime, which is the issue that is significant.

If σ denotes the standard deviation of a cross section of size N and our regression shows us a negative coefficient, then it is correct to assume that this group of OECD member country economies only have β-conditional convergence. However, it is not possible currently establish definitive conclusions about relationships between the Chilean GDP and the OECD countries´ GDP evolution without analyse carefully dispersion among productivities. In fact, in the area of analysis of APL evolution, evaluate the convergence that we are looking for would require that we focus on investigating

140 Some studies of productivity in Iceland found that increases in this last period were highly influenced by characteristics of the financial sector, and power generation and public utilities (Jónsson, 2006; Danielsson, 2008).

whether the dispersion and inequalities between APL of OECD member countries fall over time and analyse if that evolution affect the evolution of GDP.

4.8. The Falsification of the Hypothesis of σ Convergence

As shown in Quah (1993), a negative correlation is perhaps only the fulfilment of the fallacy of Galton and not a result of a distribution of countries that meet the convergence criteria; as he said: "a negative cross-section regression coefficient on initial levels is, in fact, perfectly consistent with the absence of convergence" (op. cit., page 2).

This negative correlation may be caused by deriving dynamic implications of the static behaviour of the distribution of countries at the time, when it really shows the countries' distribution over time.

Although in our sample the behaviour of product and productivity conform to neoclassical predictions of β convergence, they show a pace of dispersion far from fitting its criteria. In fact, the growth rate of the OECD countries' GDP per capita is nowhere near approaching the OECD average, but this dispersion is not measured by β convergence but the σ convergence.

The σ convergence is the concept connected with decline over time of per capita income dispersion of annual cross section data of the countries surveyed. That means that the variance approximates monotonically (with $\beta > 0$) at steady-state, which is growing in $2\sigma\mu$ value, but decreasing in β.

The extent of this dispersion can be obtained by estimating the sample variance of the logarithm of income per capita in these countries. Sala-i-Martin (2000) showed that the steady-state dispersion diminishes when β increases, but increases the variance of the disturbance with $2\sigma_{\mu}$. In other words, depending on if the initial value $2\sigma_{0}$ is below or above its steady state value, variance will be growing or decreasing in time.

Generally, β-convergence is associated with the presence of a linear function of negative slope and σ-convergence is defined as lowering of variance of real GDP per capita logarithm among economies in time. If we are presuming to falsification of the neoclassical convergence hypothesis, the differences between the two concepts force to us to inquire if both approaches lead to the same or different conclusions. Based

on this and on the distinctions between different types of convergence mentioned above, we conclude that σ is the appropriate concept of convergence that we must use when we are trying to estimate the cross-sectional dispersion of Chilean GDP and APL from 1990 to 2009.

A straightforward way to identify sigma convergence is to plot the standard deviation of the log of GDP per capita against time and if it shows a decreasing trend then there is sigma convergence. (Dalgaard and Vastrup, 2001).

Given that the confluence of data around the average is equivalent to the presence of σ convergence, a growing standard deviation can be interpreted as a sign that we are moving in the opposite direction (divergence). For this reason, we have proceeded to estimate the standard deviations of APL and growth of the GDP per capita of Chile and the other twenty-four OECD member countries, trying to establish the presence of a convergence or divergence process and then comparing our estimations of β convergence with our estimations of σ convergence.

If the variance of real GDP per capita logarithm is denoted as σ_t in group of countries in time *t,* then: we can assess that:

σ convergence among *t* and *t+1* period means: $\sigma_t > \sigma_{t+1}$

and

σ divergence means: $\sigma_t < \sigma_{t+1}$

The standard deviations of OECD GDP and APL growth rates (from 1989-1990 to 2009) are reported in the column N°2 and N° 4 of Table 4.2 containing the standard deviation of log values of growth rates of GDP per capita and APL of OECD countries during the 21 years that we are analysing.

Columns N° 3 and N° 5 report the series of Average rate of Growth of those variables.

Additionally, Figure 4.2. data shows graphically the performance of standard deviation and average growth rates of both variables.

Table 4.2. Standard deviation and average GDP per capita and APL, 25 OECD member countries: 1990–2009.

Year	GDP pc Growth	Standard Deviation of GDP pc Growth	APL Growth	Standard Deviation of APL Growth
1990	23.901,32	7.505	30,86	9,34
1991	24.069,04	7.800	31,46	9,75
1992	24.212,64	7.800	32,12	9,85
1993	24.325,25	7.921	32,79	9,99
1994	24.957,71	8.184	33,53	10,48
1995	25.550,95	8.114	34,00	10,38
1996	26.125,57	8.151	34,63	10,48
1997	27.031,48	8.462	35,62	10,58
1998	27.849,64	8.821	36,14	10,77
1999	28.739,53	9.389	36,69	11,15
2000	29.810,82	9.938	37,79	11,45
2001	30.205,28	10.081	38,28	11,52
2002	30.576,07	10.294	38,97	11,66
2003	30.911,46	10.281	39,60	11,75
2004	31.735,96	10.535	40,49	11,86
2005	32.445,44	10.863	41,14	12,07
2006	33.294,20	11.141	41,75	12,02
2007	34.168,38	11.609	42,32	11,78
2008	33.870,15	11.285	42,02	11,42
2009	32.342,80	10.662	41,86	11,47

Source: Author´s elaboration using OECD databases (2010).

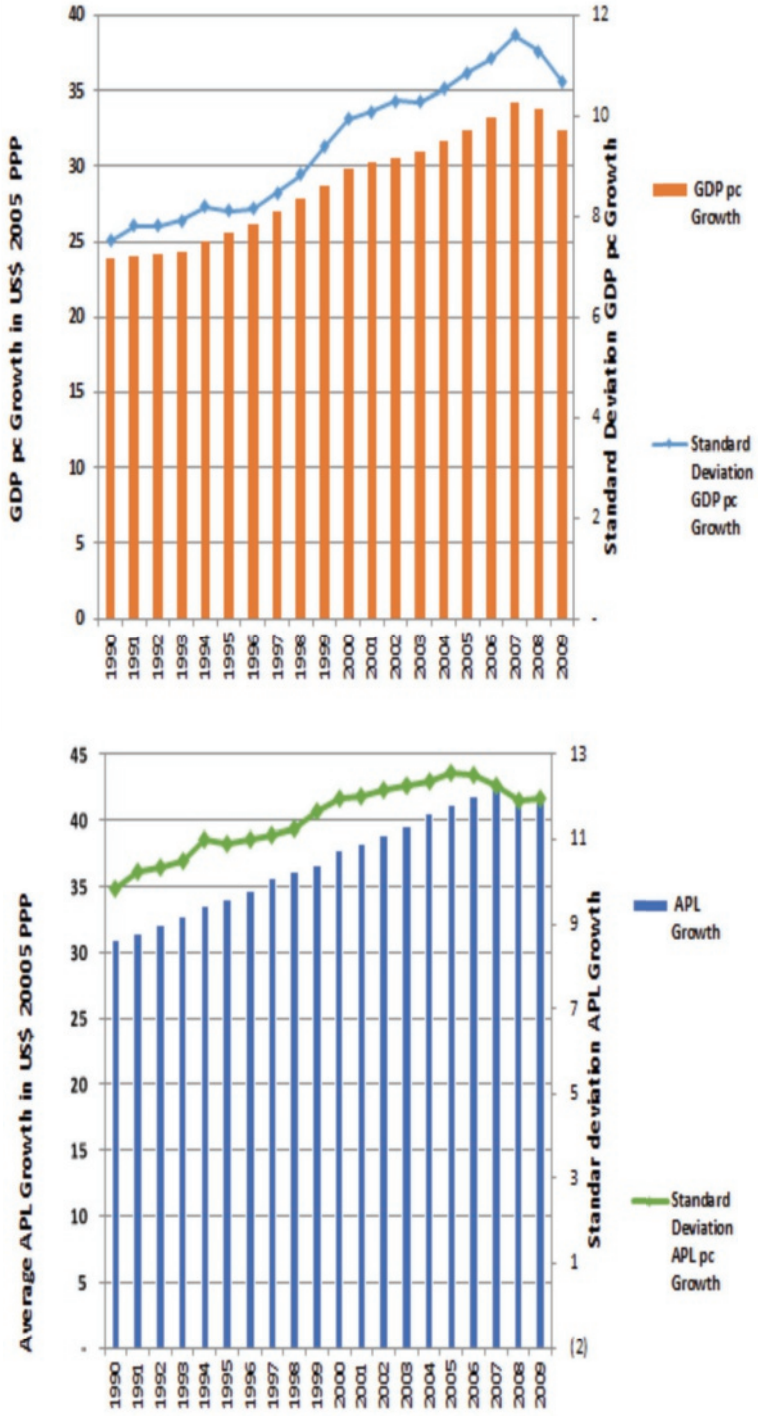

Figure 4.6. GDP per capita and APL s convergence of OECD member countries and Chile 1990-2009. Source: Author´s estimation using OECD Data bases.

If we analyse the behaviour of the standard deviations of the rates of growth in average GDP per capita and APL across these 25 countries (shown in able 4.3 above), it is clear that σ is rising.

Overtime.[141] The evolution of dispersal clearly shows that in the OECD countries analysed: $[\sigma_t < \sigma_{t+1}]$ which means that we would be in the presence of a sigma divergence, based on the clear trend of GDP per capita and APL to increase dispersal along the time.

In Table 4.3 it is possible to deduce the clear presence of σ divergence in the GDP and productivity growth. Nevertheless, while the standard deviation of both variables tends to increase in relation to their average over the period, over the last year of the period the GDP and APL decline significantly without change to the general tendency.

141 Towards the end of the period-analysed (2009), 96% of the GDP per capita of each country of the samples was twice as low as the standard deviations of the average GDP of the concerned 25 OECD member countries (See Appendix II), from which the statistical significance of these standard deviations can be deduced. Observing the growing trend amongst them, we can assert that it is not possible, because of this, to probe the hypothesis of σ convergence.

Table 4.3. GDP Per capita and APL: Convergence and Divergence in OECD Countries

Country/Time	GDP pc Indexes using ppp US$ 2005			Process of Convergence/ Divergence	APL pc Indexes using ppp US$ 2005			Process of Convergence/ Divergence
	1990	2009	1990-2009		1990	2009	1990-2009	
Australia	103,64	111,84	8,20	**Diverge**	100,45	102,71	2,26	**Diverge**
Austria	106,43	107,33	0,90	**Diverge**	105,36	104,62	**-0,74**	Converge from Above
Belgium	104,99	100,24	**-4,75**	Converge from Above	128,97	124,21	**-4,76**	Converge from Above
Canada	113,12	106,75	**-6,37**	Converge from Above	104,02	98,41	**-5,61**	Converge from Above
Chile	28,27	42,84	14,57	Converge from Below	28,84	41,56	12,72	Converge from Below
Denmark	106,47	98,84	**-7,63**	**Diverge**	112,77	106,54	**-6,23**	Converge from Above
Finland	96,82	94,12	**-2,70**	**Diverge**	87,17	97,94	10,77	Converge from Below
France	101,77	90,50	**-11,27**	**Diverge**	118,27	116,81	**-1,46**	Converge from Above
Germany	108,38	99,52	**-8,86**	**Diverge**	115,68	115,13	**-0,55**	Converge from Above
Greece	71,23	78,23	7,00	Converge from Below	69,99	69,03	**-0,96**	**Diverge**
Iceland	107,25	105,19	**-2,06**	Converge from Above	86,52	97,70	11,18	Converge from Below
Ireland	78,30	111,92	33,62	Converge from Below	83,60	113,46	29,86	Converge from Below
Italy	99,29	82,64	**-16,65**	**Diverge**	106,93	89,81	**-17,12**	**Diverge**
Japan	110,90	91,63	**-19,27**	**Diverge**	81,01	81,22	0,21	Converge from Below
Netherlands	109,97	112,95	2,98	Diverge	134,15	122,54	**-11,61**	Converge from Above
New Zealand	80,06	78,28	**-1,78**	**Diverge**	78,09	70,47	**-7,62**	**Diverge**
Norway	135,41	145,91	10,50	Diverge	146,14	150,49	4,35	Converge from Above
Portugal	67,60	66,09	**-1,51**	**Diverge**	61,57	60,19	**-1,38**	**Diverge**
Spain	82,40	83,70	1,30	Converge from Below	103,04	89,10	**-13,94**	**Diverge**
Sweden	102,79	99,86	**-2,93**	**Diverge**	98,51	105,34	6,83	Converge from Below
Switzerland	142,29	117,61	**-24,68**	Converge from Above	114,71	102,24	**-12,47**	Converge from Above
Turkey	33,11	35,93	2,82	Converge from Below	46,01	51,60	5,59	Converge from Below
United Kingdom	97,70	100,42	2,72	Converge from Below	97,86	104,86	7,00	Converge from Below
United States	133,16	127,70	***-5,46***	*Converge from Above*	124,11	130,66	6,55	**Diverge**
OCDE Average Index	**100,00**	**100,00**	**100,00**	**OCDE Average Index**	**100,00**	**100,00**	**100,00**	

Source: Author's elaboration based on OECD data.

This only marks a change in the progression of the divergence and not a change in the sense of it, given that changes are not in the direction of reducing the dispersion, but rather just in the intensity of observable dispersion, when we compare the evolution in time of both variables. Behind this aggregate data depicting a process of divergence within the supposedly more homogeneous of all world business groups, are marked differences between countries. It is necessary to distinguish those cases in which the aggregation hides the convergence of a few countries behind the divergence of others.

When we analyse the evolution of both variables, country-to-country, it is clear that there coexists a very heterogeneous process of convergence and divergence. The processes of convergence can be established because some rich countries tend to decelerate their growth rates of product or productivity in relation to OECD average growth; or because some poor countries significantly accelerate the rate of growth of these variables with respect to this parameter.

The same occurs with divergence processes. In some countries, this is due to the decline in the growth of GDP or APL that occurs because the country moves upward from the path of convergence of other countries. In addition, it occurs because the growth rate of those variables has slowed, to the point of placing it low in the path of convergence of the remaining countries when considered as a whole.

If we assume that the steady state to which OECD converge is average GDP per capita and APL expressed in PPP at constant prices we can proceed to recalculate those dynamic values assuming that OECD average would be equal to 100, year to year.

Table 4.3 shows that there are significant differences in the performance of different countries, and even in the evolution of productivity in relation to GDP per capita evolution. In terms of the dispersion on the evolution of the GDP per capita from Figure 4.2, it is clear that OECD products diverge, but that is only an average. Within OECD we can observe that 13 countries diverge and 11 countries converge.

This last group include nine large countries (Belgium, Canada, Denmark, Spain, Sweden, Switzerland, Turkey and the United States) that converge from above, i.e. recorded a decline in the growth of its GDP per capita, which leads them to come close to the OECD average. Four smaller countries (Greece, Ireland, Iceland and Chile) converge from below, showing acceleration in its growth rates which explain that GDP per capita of those countries is close to the OECD average GDP per capita.

In relation to the APL, it is observed that seven countries diverge and seventeen converge; within that last group, ten converge from above and eight from below. That shows that the convergence of productivity responds to a more extended and more powerful dynamic than the convergence of per capita product.

It is interesting to observe that, of the 13 countries in which GDP per capita converges from above, only in four (Belgium, Canada, Denmark and Switzerland) does productivity evolve in the same way, while in the 4 countries in which the product converges from below, in three of them (Ireland, Iceland and Chile) productivity also converges in the same way. In the four countries that are rising to the OECD average, is clear that GDP growth has had some effect on the growth of productivity. Nevertheless, while Ireland and Iceland are placed in close proximity to the OECD average, Greece is substantially more distant from this. Meanwhile Chile shows a productivity significantly lower than that of Greece (42 US $ v/s US $69 per hour worked). However, Chile's weak productivity is rising and the stronger productivity of Greece is clearly declining in absolute terms.[142]

All those indicators suggest that we can refute the hypothesis null that Chile and OECD does not exhibit a σ convergence over the period under analysis. In simpler terms, this means that evidence reported here supports the existence of GDP per capita and APL σ convergence of Chile and this group of OECD countries, at least in the way in which neoclassical economics define both kind of convergence.[143]

142 Convergence from above implies that there is over-capitalisation, but this term only has meaning relative to the level of productivity. If there were a higher level of TFP then the level of capital per worker would no longer be too high. On the other hand, convergence from below implies a country can develop through financial means and has a high enough level of TFP to sustain capital accumulation. By this argument, an overcapitalized economy is the same as one, which has too low factor productivity. In the end, over-capitalisation and insufficient TFP are just two sides of the same coin (Del Vechio, 2014).

143 Although Parente and Prescott (2003) report that the standard deviation of the logarithm of per capita income of 29 countries for which information is supplied had not changed significantly (or even decreased) which would imply the non-existence of divergence sigma. Our exercise applied to Chile and other 24 OECD countries, between 1990 and 2009, shows exactly the opposite.

4.9. Convergence and Institutions. The New Institutional Environment and the New Institutional Arrangements

Assuming then that Chile shows the presence of β convergence, but also displays the existence of σ convergence, the pertinent question is what this means in terms of an evaluation of Chilean public policies which have been trying to promote this process of conditional convergence forty years. In some respects, Chile would seem to be following the right path because given its factor endowment and initial income level, it has the characteristics required to achieve high growth rates especially by the fact that institutional variables which, in agree with the neoliberal approach, seem to correspond to best available option to LDC like Chile.

The initial period of economic openness seems to have allowed Chile to achieve these rates (Easterly, W., N. Loayza et al.; 1997). During its so-called "golden period" (1985-1998), Chile's growth rate was at the top, worldwide. In fact, as is emphasised in the oft-quoted study by Gallego and Loayza (2002): "*The change in Chile's per capita Gross Domestic Product (GDP) growth rate between 1985–1998 and the previous fifteen years was, by far, the highest in the world",* but subsequent to the Asian crisis, these rates declined significantly.

The difficulties associated with the "easy stage" of the export led model, which do not seem to have been adequately faced by neoliberal policies, jointly to the effects of the Asian crisis, clearly marked a turning point in the until that time supposedly successful Chilean model. The aforementioned crisis was managed in a very biased way by Chilean economic authorities who introduced a bulk of contractive policies focused on small business, at the same time that large corporations were protected from the negative effects of macroeconomic policy.

Obviously, those policies were strongly associated to important changes in the core rules of the game, modifying the institutional environment as a whole. Because of this, competition levels in the Chilean market declined significantly; the competitive strategies of large firms were oriented to the area of "cheap labour" and the intensive exploitation of natural resources, while the multifactor productivity of the economy remain stagnated. Certainly, other causes also determined the fall of Chile´s productivity, among them is highlighted the rising cost of energy. However, the decreasing levels of competence among companies seem to us the most important factor.

In general, everything seems to indicate that in Chile there are important institutional limits to the sustainability of a convergence tendency similar to observed during the golden period. In Chilean case, we can assume which the country may be associated to similar realities that different authors describe as characteristic of contexts of high asymmetries of power (Engel & Schweitzer, 2002).

In Chile, limits to deployment of growth´s efficiency policies are confronted with a key vulnerability. It is related to the fact that domestic elites have been implementing policies which have not been designed in function of the national interest, but essentially in function of the particular interest of larger business groups who control the national institutions in several and sophisticated ways.

Given this, even when a strictly neoclassical analysis of the presence of convergence, such as we have done here, confirms its trend occurrence, in practical terms it does not necessary imply that model´s outcomes are in compliance with the projections of the neoliberal model. This is the case that we are analysing, since the institutional variables defined from the neoliberal approach as essential, have shown to be insufficient to promote the growth process which they assume should be automatically produced.

Convergence found between Chile and the OECD partner countries during the period analysed, only indicates that Chile's economy achieved high growth rates over a relatively long period. When that tendency emerged, it fostered Chile`s convergence to the levels of GDP PC and productivity of developed countries. That is a normal situation and is not unusual which, when newcomers are compared to developed countries, in a first moment they show an outstanding performance as marginalist theory asses. However, the neoliberal projections in Chile were beyond neoclassical theory, establishing policy conclusions concerning the effect on the economy of its proposals of trade openness and liberalisation in short periods of time (Bardón et al.; 1985; Beyer, H. and R. Vergara. 2002, Buchi, 2007). However, these optimists forecast, as our estimates show, would be required, ceteris paribus, about eighty years to achieve the promised goal of convergence.

Chilean public policies were based, during the first phase of its model implementation (1973-1989), on the general belief that if the country had trouble in obtaining its desired levels of convergence of productivity and incomes, these could be explained by the presence of an adverse role of the State, the lack of flexibilities of some markets, the low mobility of production factors or by a limited trade and capital´s openness. In

general, these market rigidities have been identified, from a neoliberal point of view, as located in areas related to property rights, international financial flows limits, and restrictions to foreign trade.

However, from 1990 onwards, the new economic authorities did not associate the presence of an elusive convergence of GDP and APL with the weak export orientation of Chilean firms, or to the oligopolistic character of market structures in the Chilean economy. Nor did they assume that the fact that access to credit was abnormally concentrated in large business groups was a serious issue. Finally, they did not consider that the enormous amount of FDI in the mining sector was inducing a form of "Dutch Disease" in the Chilean economy (Palma, 2013; Martner y Rivera, 2013*)*. On the contrary, their diagnosis was strongly influenced by TWC's point of view: that sustained that trade openness and market liberalisation were not yet radical enough, and liberalisation and deregulation were also insufficient in the different sectors of the economy.

In sum, the new Chilean authorities accepted (from 1990 to 2009) that the core of the recently elaborated TWC institutional prescriptions (1989), was the desirable path to be followed by the Chilean economy and which, if the price system become free, the institutional environment and the institutional arrangements cannot be other think, that the optimum ones.

When TWC recommended that Chile implemented more of the same Neoliberal prescriptions already applied during the last seventeen years by the country, the impressive growths rate exhibited at that time by the Chilean economy seemed to give strong support to this approach. After that, any criticism of the neoliberal model that began to be voiced within the ruling coalition early on was considered "highly ideological" and therefore disposable.[144]

Following this line of analysis and according to the results of our tests of convergence, it would appear that in Chile, at least, there seemed to be the well-established presence of a positive relationship between trade liberalisation and GDP per capita growth based on the aforementioned causes. Nevertheless, the presence of β and σ convergence only reflects in a very general sense the evolutionary perspectives of the Chilean model in comparison of the OECD parameter. Even when only the APL and GDP per capita

144 See: http://diario.latercera.com/2012/06/22/01/contenido/pais/31-112030-9-manifiesto-reimpulsa-disputa-entre-autocomplacientes-y-autoflagelantes.shtml.

of Portugal or Greece are used, Chile shows a distance too wide from such countries to enable certainty of reaching that benchmark in a reasonable period.

The key to trade openness, under the usual neoclassical assumptions, is about the properties of technology and the technological diffusion. The ability to adopt low-cost techniques developed in more affluent regions, is crucial to those countries that enter freely into a fully open economy, through the import of such technology and the incorporation of FDI.

Individual firms will initially absorb the impact of openness and from there changes would be induced to the sectorial structure of employment and production, eliminating sectors and firms of low productivity level that would normally reduce the GDP level, and generating new opportunities for growth by labour reallocation to more productive sectors.

Notwithstanding Chile's disciplined application of orthodox neoliberal guidelines, then TWC prescriptions, the general trend of Chilean GDP and productivity growth have not been able to generate the concretion of such convergence after almost 40 years of trade openness and market liberalisation.

Even when our research reveals that, Chile would be moving on the road to convergence towards OECD product and productivity parameters, to move in the direction of this target it is not a simple task given that objective is s very distant and the country is extremely liable to the impact of external shocks, changes in the price of exports and various others factors related to the low competitiveness of domestic markets. In other words, the road seems to be correct, but the car intended to travel it does not have the necessary power and, as we will discuss later, has the wrong road map.

This situation seems to suggest that, throughout the analysed period, the institutional environment was well associated to consolidation of trade openness and market liberalisation and, sometimes, to maintenance of high growth levels of GDP per capita and productivity. However, preservation of that institutional environment was unable to sustain these growth rates beyond the golden economic period.

Because of that, assessments used by post dictatorship governments to assess that it would be inconvenient for Chile to discontinue its support of the implementation of the macro-institutional reforms promoted by TWC and adopted by post dictatorship

governments lack of solid grounds. If we conclude that neoliberal reforms would consolidate a path that leads Chile towards economic convergence, the correct path would be to follow this TWC guidance. However, if it is not the situation, that kind of endorsements would be highly dysfunctional to the growth goals of Chilean economy, giving that following these prescriptions, convergence became hard to be reached.

This is a relevant discussion when debating the Chilean case. In Chile, an export led model seemed to be a good option for producing, under specific circumstances, GDP growth rates of note as some authors highlight (Lefort, 1997). The same can be said about market liberalisation, but it is clear that this path of growth is not strong enough to become sustainable and to drive the country towards development. The final answer seems then to be in the field of convergence´s sustainability, specifically in the causes that have led to economic growth that has made it possible for Chile to achieve in some points of the time exhibit some convergence trend, but not to sustain it long or even medium term.

4.10. Conclusions

The analysis of the Chilean experience shows that GDP and productivity growth are the result of a diverse set of factors, which interact in more complex and multifaceted ways than linear relationship between prices, efficiency and economic growth, as suggested by neoclassical theory and in which neoliberals fervently believe.

Developing countries that have opened their economies have tended to produce an (not immediate) acceleration of its growth rate; in general, they have gone from an average annual rate of 1.4% in the 1960s to one of 5% in the 1990s (Lindert and Williamson, 2001). In the Chilean case, this tendency has been reproduced. When Chile opened its economy to global markets, their income level started to converge towards the GDP and productivity of advanced countries after a period of ten years, in a manner analogous to the predictions of neoclassical economists (Dollar, 2001).

We cannot deny that the strong growth experienced by the Chilean economy and its high growth rate during the period 1985-1998 have enabled a significant convergence of both its GDP per capita and average labour productivity with those existing inside the OECD. This is independent of the mode of convergence used to demonstrate this. However, the Chilean experience does not fit at all with the predictions of the

neo-liberal economists (and also shared by several left-wing economists) who has been waiting that integration of Chile with the most advanced countries through the trade liberalisation processes, would accelerate the domestic growth rates permanently, improving the country income´s level. In that form, they expected that in a short period, Chile should converge towards the income level of the advanced countries.

Is from this belief in the capability of Chilean model to produce high growth rates, where apparently also the high reputation of the neoliberal model applied in Chile lies. However, our findings show convergence during some periods of high growth, but also that, in the medium and long run, this trend is not strong enough to sustain significant levels of convergence, because of the volatility and weakness of the economic growth processes.

We have also been able to establish that the Chilean economy, despite its high degree of openness and liberalisation, has failed to install persistent and systematic processes of growth of GDP and productivity.

In the Chilean case, the good performance of markets requires a fair competition framework and fair market arrangements. An economy whose GDP is 80% controlled by thirty business groups is not a situation that may be explained by the new trade theory approaches that sustains that, in some context, is more efficient for an open economy promote the development of the firms which are closest the technological world frontier. These business groups hardly may be defined as on the verge of technology and innovation, and their impact on the economy as a whole has been unable to push-up the GDP growth process and the TFP of the Chilean economy. Then, if economy do not deal in an adequate way with both institutional aspects, even when would be functioning a context of trade openness, markets may perhaps fail and produce inefficient ´s resource allocation. Moreover, it is possible that the distribution of nationally produced wealth may be misappropriated by a few business groups of great market power which, control economic and political institutions. Our conclusion is that the Chilean situation closely resembles this situation.

The rule of the Chilean economy by a few business groups, that the implementation of the Chilean neoliberal model made possible, was a process that evolved, step by step, during a long period in which at least two main phases can be distinguished in.

In the first phase, ranging from late 1973 to early 1990, the authorities´ effort was focused on the alteration of the relationship of relative prices through drastic trade liberalisation which drastically modified the former institutional environment. It was assumed that this would generate a new dynamic of resource allocation in such a way that the growth of GDP and productivity would foster the growth of the country, leading it to development and hence, to convergence with the more developed countries.

In the second phase, going from 1990 to 2009, the new authority focused its effort on the adoption of the prescriptions proposed by multilateral organisations, which reinforced the abandonment of the monetarist approach that the neoliberal model had embodied since its inception, replacing it by a less diverse but undoubtedly more sophisticated approach: The Washington Consensus. This model tried to incorporate ten conditionality arrangements of clear neoliberal sign, which should be adopted by all economies, which like Chile, hoped to converge to the levels of productivity and product of the OECD.

In the course of this new phase, Chile further deepened its trade openness, which began to operate through bilateral treaties of free trade and not through a unilateral opening, as had happened during the monetarist period. Similarly, the entry of Chile into this dynamic was strengthened by their incorporation by the OECD in 2010; start to introduce in Chilean economy a new set of institutional arrangements which deepened the neoliberal character of the Chilean model of development. However, the inadequacy of the ten conditions promoted by TWC, which were assumed by Chile in 1990 and which are have been applied for over 25 years, simply formalised a situation inherited from the neoliberal-monetarist period.

With more or less orthodoxy, despite the previously reported country's deviations from the norm, the bulk of the 25 countries surveyed and reported in this chapter, have remained within the ranges accepted by the organisation. On the other hand, only 13 of them converge to the OECD average and 12 do not. We can then conclude that, regardless of the existence of an inverse relationship between level of initial GDP per capita and GDP growth, as well as presence of similar institutional environment and related institutional arrangements, convergence is not per se guaranteed to all these countries.

Nevertheless, to define those institutional variables that determine the initial strong speed of growth and later weakening remains yet as an incomplete task. It will be

addressed in Chapter VIII. In this respect, the most remarkable conclusions to be drawn from the analysis already developed in this chapter are as follows:

- After 1990, Chile endorsed all the institutional prescriptions of the Washington consensus, which was transformed, after the end of the dictatorship, into the successor to the neoliberal-monetarist approach that proceeded as the strategic driver of the Chilean economy. After this, Chile exhibited a general but weak tendency of convergence with the other economies of the OECD as it was predicted would happen. However, that tendency was strong only during slightly over a decade, weakening after this golden period.
- In general, both in the area of GDP per capita growth as on the Average Productivity Growth, the presence of some kind of conditional β convergence among the 25 OECD member's countries surveyed (Chile included) can be accepted; but not all OECD countries are converging in a similar way to a unique product or productivity level. Even Chile converges more quickly than the rest. The high growth rates that permit this correspond only to the golden period of its development (1985-1998). Although projected over long periods, Chile has not produced the power needed to converge in decades toward the average level of the OECD member countries. The goal to converge in the next few years with the level of the poorest of the 25 OECD countries surveyed (Portugal) is not at all assured and seems more distant every day.
- Chile has been extremely rigorous in the implementation of the institutional policies promoted by TWC, allowing its promoters and advocates of neoliberalism to predict a rapid growth of GDP and productivity level. The presence of β conditional convergence shows that the country does present, at least during a decade, a strong correlation between high GDP per capita growth and the accomplishment of TWC conditionality conditions. However, the decreasing speed at which Chile has been increasing its GDP and the lack of productivity growth, lets predict which, during the next decades the current economic institutions do not be able to sustain growth and development process. Chileans institutions have not possessed sufficient strength and speed to close, in a short period, the gap with the remaining OECD member countries previously analysed. This contradicts what has been forecasted by successive Chilean post-dictatorship governments and by neoliberal scholars and politicians.
- The findings of our research about evolution of GDP and productivity growth in the 25 analysed OECD countries, show that they exhibit a growing level

of dispersion around their average levels of GDP per capita and productivity. Although there is a clear β conditional convergence in this group, σ convergence clearly does not exist. This happens because the two proposed explanatory variables (level of base GDP and TWC conditionality) may not be necessarily the variables that explain Chile's high GDP growth, nor its subsequent deceleration. The Chilean case is markedly different to the others 24 countries. For that reason, it will be necessary to develop, a deeper exploration on the grounds of that situation in the following chapters.

- We can also conclude that, analysing the data of period 1990-2009, it is not possible to reject the hypothesis that Chile is converging with the other OECD member countries in terms of product or in productivity. However, both kinds of convergence are weak and volatile. The convergence tendency is only plausible if the average GDP and productivity similar to be registered during the golden period, would be assumed as an invariable tendency for the next two additional decades. Nevertheless, given that from 1997 onwards both processes lose energy, the convergence tendency has diluted its initial impulse.
- Considering only the average tendency, that is highly affected by the influence of the twelve years of declining evolution of Chile's GDP growth and APL convergence is already not a clearly plausible goal.
- The target of full convergence would be achieved, according to neoliberals, by a combination of macroeconomic equilibrium with changes in relative prices induced by trade openness and followed by a process of liberalising and resizing of the state role. This would automatically result in a better allocation of resources. This concept is associated with a second neoliberal appraisal: the only institutional elements that can positively affect the process of allocation of resources are those related to the introduction of new rules of the game that foster the "free" operation of the already existing markets. However, this neoliberal assessment seems to be only a rationalization of the presence of an institutional environment that sustains operation and consolidation of markets that are not fully competitive and that are granted by institutional rules appropriated only to economic concentration, but no to GDP and productivity growth.
- The outcomes of the Chilean model regarding convergence show that the old monetarist neoliberal model was unable to accomplish their forecast and promises. However, the adoption by the new Chilean authorities of TWC institutional prescriptions, induced the application of public policies whose declared goals were clearly not fulfilled but, that produced high concentration

indexes. This concentration produced an unbalanced market power of the large business groups, a state of affairs that engender a top-heavy political influence of them, manipulating to the successive post-dictatorship governments in order to adapt their economic programme to the new neoliberal institutional framework.

- The Chilean Model outputs does not fit with the neoliberal promise of strengthening of an economic dynamic of inclusive character. On the contrary, its characteristics appear to be highly exclusive and viable only within a context of the survival of the institutions created by the military dictatorship. The continuity of the neoliberal model of development, as well as boundaries to the growth and development of the country after the end of dictatorship period, are highly correlated phenomena. Both of them may be attributed to the lack of real commitment to developing institutional changes that the centre-left political forces- sometimes opposed to the neoliberal model- declared (before 1990) that they were willing to promote once they reached the government, but were postponed after they took control of government.
- A deeper analysis of these issues will be developed with more detail in Chapter VIII. At this time, we only have presented the point as a primary conclusion from which we will make a deeper analysis appraising the microeconomic evolution of the Chilean economy throughout the period under study, comparing the observed results with the predictions made by the neoclassical-neoliberal theory in respect to these and other variables.

Chapter 5

The Impact of Openness Liberalisation on the Resource Allocation Mechanisms of the Chilean Economy

The objective of this chapter is to analyse the new system of relative prices installed by the trade openness and its relationship with the economic concentration and the diffusion mechanisms of technological progress within the Chilean productive fabric. Aiming to analyse if the new prices have actually been acting as signals able to efficiently orientate the resource allocation process of the Chilean economy, or if in the opposite direction, resource allocation is a process determined by the institutional structure of the Chilean economy. We also analyse the role that two contradictory forces are exerting on the diffusion of technical progress of Chilean economy during the trade openness and liberalisation process. On one side, we analyse the actual characteristic of market competition process installed by trade openness. On the other side, the characteristics of the concentration process that have structurally limited market competition. Then, we will analyse the role that both forces play encouraging or suppressing the economic efficiency in domestic markets.

5.1. The Boundaries of Price Signals as Mechanisms of Resource Allocation

As expressed in our working hypothesis, the supporters of neoliberal economic model applied in Chile held that:

> *"Chilean economic trade openness and market liberalisation made it possible for the Chilean economy, from 1973 onwards, to equip itself with an adequate macroeconomic environment and a pricing mechanism that ensured an efficient resource allocation mechanism. As a result, the Chilean economy produced a reallocation of its factors of production (capital and labour), from its most backward toward the more productive and globalised sectors.*

The available information, before and after 1990, does not seem to fit with this optimistic sequence of events.

From an academic perspective, the stated objective of the neoliberal model of development was that, the reform process would allow the Chilean economy converge, at some moment of history, to its own steady state of development, defined as so close to the level of the less developed European OECD countries. However, fulfilment of that academic hypothesis would require that trade openness actually may induce a more efficient resources allocation process in which, productive convergence should be a viable reality; nevertheless, it is not clear that this happened in the way in which it was proposed.

At the political level, the neoliberal promise was that through economic reforms, Chile would move to the status of a developed country in the course of a single generation. The basis of that promise was that markets without regulations and an economy free of state interference, would fulfil the total potential for the reallocation of resources, thereby sustaining the high growth rates necessary for achieving the model´s aspirations.

Towards the end of the 1980s, it seemed clear that the high rates of growth exhibited by the Chilean economy were taking the country in that direction and that in 20 years the ambitious objectives of the model could be fulfilled. However, contrary to the professed willingness to create more efficient, transparent and competitive markets, Chile seemed to have consolidated a context in which national markets operate very different to neoliberal forecasts.

In order to deepen the analysis of these problems, in first place, this chapter will try to investigate whether trade liberalisation has resulted in a better capacity of resource allocation within the Chilean economy or in more efficient production´s factors utilization. In second place, we will analyse if the new characteristics of the resource allocation process are actually depending of the new system of relative prices produced by trade openness. Nonetheless, the impact on the price system relies strongly on the market organizations that govern it.

5.2. Has the Chilean Price System been adjusted to international prices as a result of market liberalization?

It is generally assumed that if the number of participants in a market is large, they would find it increasingly difficult to collude (Clarke and Davies; 1982; Helpman and Krugman, 1989). Thus, without collusion, competition will prevail and lower prices would be propagated in such markets.[145] An extension of this hypothesis is that in an open economy that exponentially increases its number of participants in tradable product markets; the international competition would produce a greater economic efficiency (Tybout et al., 1991).

If these forecasts are well-founded, and both external inflation as well as international prices and costs must pass on to domestic markets, one to one,[146] then influence exerted by trade openness on the tradable-goods price index must be greater than the effect on the non-tradable products price index. This last one is composed of products which

145 In recent years, having gained a certain academic popularity, theoretical approaches of neoclassical-non-neoliberal root, which argue that the lack of competition in the markets is not in itself harmful to the economy. On the contrary, it is argued that, on certain occasions, economic concentration could be a good vehicle to: 1) generate economies of scale in large business groups that compete globally. 2) promote innovative companies that need to capitalize their R & D & I cost, counting with windows of time in which they can "escape competition" 3) Focus the productive effort of the economy in companies near global borders of productivity, avoiding supporting small and weak defiant firms whose feeble competitive capacity would damage the economy as a whole, by eroding the dominant position of the most innovative and advanced companies. This point of view from which we clearly disagree, because we consider it is not applicable to the case under study. Will be analysed this issue in greater detail in the final sections of this chapter.

146 That would mean that the elasticity of transmission, defined as the percentage change in the price of a good or service in the domestic market given a change percentage (1%) on the price of the same good or service in international markets would be equal to one.

are less affected by trade openness and more affected by institutional arrangements. Therefore, given the prevalence of new international prices associated with multiple and competitive providers, a highly elastic demand curve should characterise domestic consumer preferences of tradable goods, allowing international price signals to become more powerful than any arrangement in domestic markets.

The neoliberal view emphasises that in full open markets with high price elasticity, minimal price changes of imports would induce relevant changes in the quantities demanded, whose limits are determined by several factors: consumer preference, the level of income of the economy and - ceteris paribus a certain exchange rate - the availability of foreign currency that the economy makes available to consumers. All those factors depend on specific arrangements to be established in domestic markets, but from the neoliberal approach those are only viewed as a by-product of trade openness and free market operation.

According to this approach, eliminating or reducing import tariffs to almost zero per cent, as happened in the Chilean case (see chapter II), should allow variations in international prices to be fully transferred to the domestic markets. Given the neutrality of market induced arrangements and following their argumentation, the variations in international prices should transform over time into the price convergence of a similar basket of products.

These adaptations would be the result of arbitrage actions that should emerge and that would encourage price equalisation between Chile and its main trade partners (i.e. the law of one price). Nevertheless, it is accepted as fact worldwide that prices of the same goods across countries (expressed in the same currency) not only differ, but also differ widely and persistently. (Goldberg and Knetter, 1997; Ravn, Schmitt-Grohe and Uribe, 2006; Crucifix and Shintyan, 2006).[147]

147 According to neoclassical economic theory, the possibility of arbitrage in tradable goods ensures that prices are equivalent in different countries. Under some additional assumptions, such as a fixed exchange rate and the absence of transaction costs, perfect arbitrage involves the automatic transmission of international price changes, as well as the instant effects of nominal price to exchange-rate adjustments. This ensures that each product would have a single price worldwide. This conclusion, known in the literature as "Law of one price" (Krugman and Obstfeld, 1992), is not shared by many neoclassical economists even when for neoliberals who believe that, the aforementioned mechanics of " market-clearing" in open economies are able to generate efficient equilibrium in the long term. Moreover, they think that prerequisites of field operation of the "Law of one price" would be the presence of domestic price flexibility (upstairs and downstairs) and the presence of international transport that operate in a

In the real world, transmission mechanisms are distorted by several causes of institutional order; conformation of oligopolistic market structures amongst others, which are very common in markets like Chile in which competition is weak and opaque but strong barriers exist to market entry. In spite of this, neoliberal advocates of the Chilean model assume that, the presence of "right prices" must be an outcome derived from the fact that trade openness would transform internal markets, making them more competitive. That process would be additionally promoted by attracting foreign investment and creating endogenous incentives to improve the productive process.

After installing these new "right prices", it would be logical to expect a fast emergence of factor reallocation from the most inefficient and unproductive sectors to the most efficient and productive ones. Furthermore, if the factors of production were remunerated according to their value of marginal productivity (VMgP), the result in the labour sphere would be an increase in worker remunerations associated with productivity improvements. Symmetrically, in the sphere of capital, there reallocation should be induced towards more profitable economics. If mobilised, capital increases productivity, inducing better management and/or technological innovations. The result should be an enhanced level of production and capital remuneration.

In other words, from the neoliberal view, full trade openness and market liberalisation are the only sensible grounds for a model of development that effectively aspires to the dissemination of technical progress and production of a virtuous relationship between growth and equity, understanding this last one as equality of opportunities at the market. For them, the institutional issues are only a by-product, or a marginalised factor of small relevance. But, even from within the neoclassical perspective, there are different opinions about this point of view.

Sir John Hicks (1935) was one of the first to propose the hypothesis arguing that markets do not behave precisely in the way described by neoliberals. He suggests that the greater the market power of the firm, the lower its management effort to maximise operational efficiency will be, producing a negative correlation between those two variables. This is due to a low level of market competition produced by the underestimation of the role of antitrust institutions.[148]

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competitive manner.

148 In Chile during 1990-2009, economic concentration was intensified because of the public policies of post dictatorship governments, which actually underestimated the effect of the institutional

If we carefully review the process of the opening of the Chilean economy, the conceptualisation of the real relationship between market power and firm efficiency proposed by Hicks could be well-suited to the situation under study.

Given the small size of its economy, with the exception of the copper production, Chile acts as price taker in practically all the international markets in which it participates. Thus, the tradable goods inflation, essentially related to international prices performance, will tend to be smaller than inflation of non-tradable products that are less affected by low international prices. Subsequently, if the economy can consolidate a growing influence of tradable products on the consumer price index, equalising domestic prices to external ones, Chile would display high levels of alignment between its international and domestic prices.

To enquire whether the Chilean economy actually validates this trend as to the equalisation of prices, it is necessary to falsify the whole neoclassical-neoliberal hypothesis that holds that trade liberalisation tends to:

1. Align domestic prices to international prices,
2. Introduce greater competition in domestic markets
3. Introduce more productivity in the economy as a whole, since it identified international prices as operating in a way that is very close to "efficiency prices", fostering a better allocation of resources in the economy".

The falsification of the previous hypothesis requires specific instruments enabling some measurement of these three variables: alignment, competition and efficiency. Based on their behaviour it will be possible to deduce, firstly, if trade opening produced an alignment of domestic prices in relation to international prices and if it effectively promoted greater competition in domestic markets, and so had a tendency to produce

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arrangements expressed in the weakness of antitrust legislation and their enforcement organizations, a legacy of dictatorship which was imbricated to the concentrator function of many of the macroeconomic policies of the new democratically elected governments (Ffrench-Davis, 2003, pages 339-346). When the Chilean economy confronted external shocks (especially during the Asian crisis of 1997-1988), the macroeconomic policies were strictly pro-cyclical and heavily weighted towards larger enterprises. The consequences of the adjustment policies fell on MSME, while large companies were protected from the effects of these policies. The option taken by post dictatorship administrations accelerated a strong economic concentration giving additional market power to large business groups, mostly founded or restructured during the dictatorial period. This trend towards the concentration of the Chilean economy has operated against the expectations of the trade openness process.

a higher level of efficiency in the economy as a whole. On the contrary, if we can prove that these factors are not present, the field would be open to try to deploy other explanation that emphasizes, for instance, the relevance of institutional factors.

In the first place, in order to establish the existence of price alignment of domestic to international prices, we will describe the evolutionary trends of Consumer Prices Indexes (CPI) of Chile and CPI of their principal trade partners. On second place, we will proceed to estimate price alignment indicators that bring us a more systematic view of the real impact of trade openness on the Chilean economy pricing system. In the third place we will analyse if, after forty years of the launching of liberalization process, the Chilean economy displays a higher level of productivity.

5.3. The Evolution of Consumer Price Index

Figure 5.1 shows the evolution of Chilean general CPI in relation to foreign indexes which measure inflation of countries that are the destination of 65% of exports and the origin of over 50% of Chilean imports (DIRECON, 2015). From this figure, it is possible to visualise that during the period 1990-2009, the Chilean-CPI is fairly far above the Consumer Price Index of the USA, OECD and China, the main Chilean trading partner.

One of the main neoliberal theoretical explanations of the fact that Chilean-CPI has been growing over CPI of its main trade partners, sustains that domestic inflation must be a result of market rigidities and the rise in labour remunerations (Hevia and Nicolini, 2015). However, this assessment does not explain an empirical fact: average wage growth is lower in Chile than in wealthier countries.

If Chile, a country that has labour markets even less regulated than developed countries, shows a higher CPI than USA and OECD countries, it is difficult to assume that wage pressures are the variable that explain the presence of a larger Chilean CPI.[149] Moreover,

149 The structure of CPI utilised in this research used expenditure weights base December 2008 = 100, which comes from the Households Budgets Survey (HBS) 2006-2007. These values are centred on April 2007 and correspond to a sample of 6.753 households representing an urban population of 5,787 million people of the Metropolitan area of Santiago. Each product forming the CPI-basket has a weight that allows the aggregation of higher indices, until reaching the IPC level. The weighting is the relative expenditure (relative weight) of a product, within the total household expenditure. The Central Bank estimates a general CPI disaggregated in two sub-indexes: Tradable CPI and Non-tradable CPI. The

in addition to presenting Chile a higher inflation than its trading partners, as we can see in Figure 5.2, Chile's inflation is decreasing and relatively low. In the last years of the period under analysis it is clear that it represents a "sword of Damocles" oscillating over the Chilean economy, and therefore, the authorities have never considered it "a tame beast".[150]

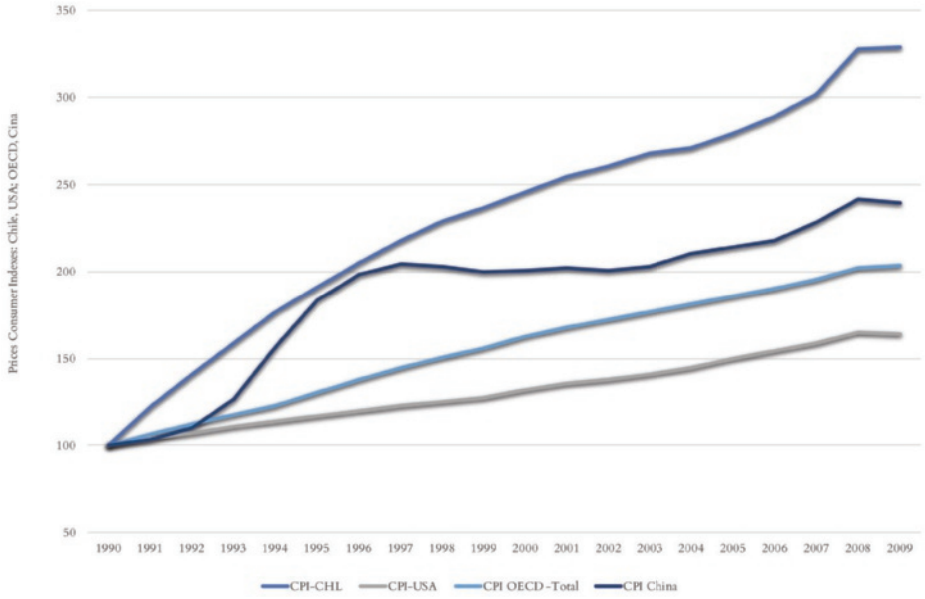

Figure 5.1. Evolution of CPI of Chile and their Main Trade Partners: 1990–2009
Source: INE-Chile and OECD. Base Year 1960=100.

The Chilean inflation growth is not a short-term process; we can observe 20 years of strong efforts from the autonomous Central Bank to control inflation evolution, which have not always been successful. If we consider the period 1990–2009 as a whole, the inflationary level defined as a target was not achieved. Effective inflation

general CPI is a weighted average of those two sub-indexes. Each product in the CPI basket has a weight that corresponds to the relative expenditure (relative importance) of a product within the total expenditure of households. This enables the aggregation of indices by product until the general index is reached.

150 This situation is endorsed by its evolution beyond the analysed period (i.e. 2010–2015). Through the period 2010–2015, in general, inflation does not differ from the level achieved the previous decade. Although in 2015, after the copper price collapsed, inducing a severe devaluation of the Chilean peso, inflation rose rapidly above the maximum level set by the Central Bank (4%), reaching 4.5% between January and September 2015.

from 1990 to 2009 was on average above 5.5% annually, evolving from 24.5% in 1990 to -1.6% in 2009.[151]

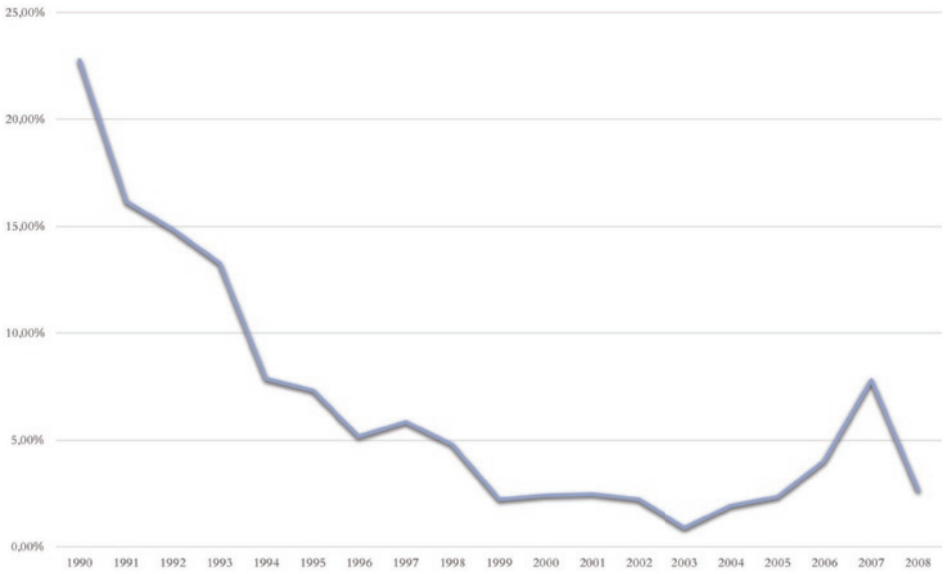

Figure 5.2. Evolution of Chile´s CPI: 1990-2009
Source: INE 2010.

At this point in the discussion, the neoliberal explanation generally focuses its short-term analysis on exchange rate effects on wages and prices (Lagos 1994:29; Lagos 2015) in order to explain the bizarre performance of domestic inflation, excessively refractory to the impact of the trade openness.[152]

151 The Central Bank of Chile policy, which during the final days of the dictatorship was transformed into an autonomous entity, has been assigned the mission of "...*look after the stability of the currency, that is, to keep inflation low and stable over time. The Bank must also promote the stability and efficacy of the financial system and the normal functioning of internal and external payment systems, predictable contributing to reduce the ups and downs of the economic cycles, thus providing a solid basis for the country´s permanent growth (given that), a higher inflation tends to distort the system of prices of the economy and therefore the information that relatives' prices deliver does not allow an efficient resources allocation." (*BCCH, 2015; Marshall, 2015). The Central Bank's inflationary target was not fulfilled during the first decade of the analysed period, in which the average annual inflation was a 10.1%, but it was accomplished during the second decade in which the average inflation was 3.2% per year.

152 Lagos (op. cit.) declares that in Chile the variations in the rate of domestic inflation are produced mainly by fluctuations in the short-run real exchange rate induced by monetary.

They emphasise that, in their view, the two variables that permeate local inflation are, firstly wage rises, influenced by the government setting of a basic wage, and secondly, the reset of automatically indexed prices (Selaive et al, 2015). In others words they assume that institutional factors which exert relevant influence on the domestic evolution process are those residual arrangements which are not yet normalized by trade openness.

Obviously, indexation cannot produce a bigger impact than inflation itself. In the worst case, indexation defines inflation´s floor and the difficulties of reducing it. Nonetheless, from the neoliberal point of view it is assumed exchange rates fluctuations and indexed salaries growing excessively would be the best explanation for the surviving price´s spread amongst Chilean and international inflation. However, the available evidence 2009 does not point in this direction.

If we look at Figure 5.3, the evolution of exchange rates (1990-2009) in relation to the labour costs and the price relationship between tradable and non-tradable products, we can observe that real labour costs have risen by 50%, the real exchange rate has been revalued by 25% and the relationship between tradable and non-tradable goods prices fell 38%. In spite of this, inflation registers an accumulated increase of 25% during that period.

At first glance, the performance of these variables does not explain the evolution of Chilean CPI. On the contrary, it is quite clear that the main part of inflation obeys the strong impact exerted by non-tradable prices on CPI evolution, given that this group of products has a clear influence on the composition of the basket of goods by which Chilean CPI is calculated.[153]

Figure 5.3, shows that Chilean CPI moves above the evolution of the other variables here considered and that, the sum of these hardly confirmed the general trend of domestic prices, because the evolution of some variables tends to compensate from the others. On the other hand, box 5.3-B shows that Chilean CPI is a weighted average of Non-Tradable Consumer Price Index (NTCPI) and Tradable Consumer Price Index

153 In 1981, a few years after the start of Chilean trade openness, the tradable products had a share of 64.35% within the basket of products used to estimate Chilean CPI and the non-tradable had a share of 36.65% (Meza, 1981). 28 years later in 2009, the tradable basket´s weight had descended to 58.15% and the non-tradable' weight had increased to 41.85% (INE, 2010).

TCPI, in which NTCPI exerts the most significant influence on the absolute values of the general Consumer Price (CPI) index evolution.

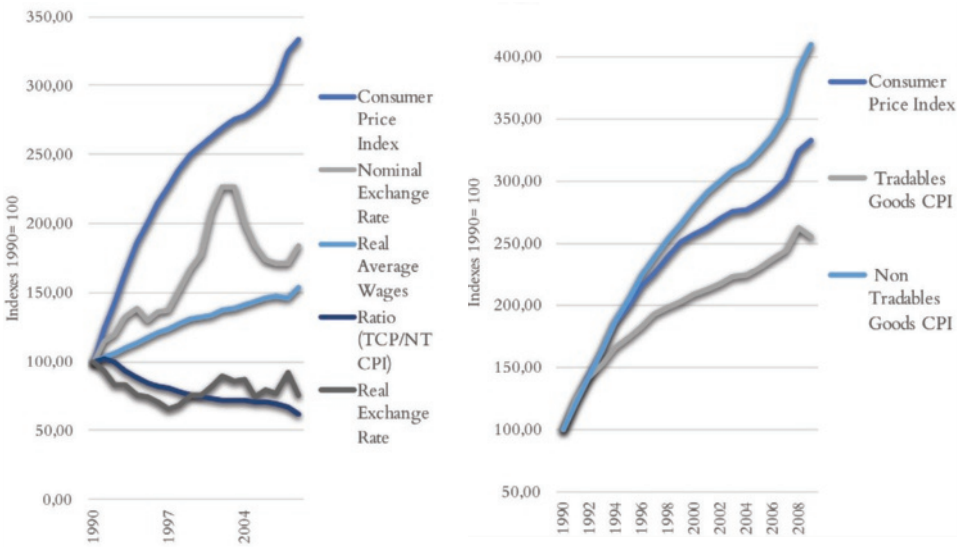

Figure 5.3. Evolution of CPI of Chile and their Possible Determining Factors, 1990–2009
Source: Consumer Prices Indexes (CPI). Historical series: data base from INE (2015). Real Rate of Change converted to base 1990 = 100. Data base from Central Bank of Chile (2015).

From 5.3.A is clear that Real Average Wages (RAW) are growing at a moderate rate (50% in 20 years) even though the starting point was at a very low level.[154] In Chile, wages still remain very near to the ground, so that the impact of the moderate pressures of cost which they have been generating from 1990, cannot reverse the fact that Chile continues being a country of cheap labour if is compared to USA or the OECD countries, which have higher wages and better income distribution.

In addition, CPI is growing faster than RAW, a fact which suggests that inflation pressures are not only originating in growing labour costs, but are mostly originating

154 We must remember that the exchange rate devaluation of 1985–1989 (the last years of the dictatorship) was the result of a strong adjustment of the public-sector expenditure with respect to the GDP and a sustained crash in real wages. Both factors permitted significant increases in GDP and the surplus in the trade balance, which was inherited by the first government post-dictatorship. If wages since then have increased below inflation, it is hard to argue that during the period under study there have been strong wage pressures influencing domestic inflation.

from other variables. From there it is clear why; by displaying the breakdown of the Chilean CPI rise between the price evolution of tradable and non-tradable goods, it is possible to observe that inflation of non-tradable has been growing much higher than the tradable goods inflation.

During the period 1990-2009, this has resulted in the level of the price of non-tradable products exerting a leading effect on Chile´s CPI evolution. For that reason, it is necessary to analyse, in a more systematic way why, despite full trade openness, Chile´s CPI behaves in this way.

To characterise this situation adequately, we will firstly establish the presence or absence of a certain alignment of domestic and international prices due to trade liberalisation and after that will we determine whether this price alignment (or misalignment) is a critical factor that explains the CPI behaviour.

5.4. Price Alignment

Firstly, we will analyse to what extent a certain synchronicity of time between the evolutions of the tradable versus non-tradable prices in relation to evolution of general domestic CPI has been present between 1990 and 2009. We will look at the behaviour of these prices, which are the two more relevant components of the CPI, to define whether this convergence is present.

If we denominate:

TCPI: Price Index for Tradable products
NTCPI: Price Index for Non-Tradable products
ICPI: International Consumer Price Index relevant to Chilean foreign trade
GCPI: General Consumer Price Index, ***t*** is year of observation; and ***n*** the number of observations.

On that basis, we can estimate the values of at least three Price Alignment Coefficients (which will call PAC) whose estimate allows us to observe the behaviour of the prices of both types of goods (tradable and non-tradable) in relation to general CPI and behaviour of general CPI in relation to international inflation. The three aforementioned PAC will be expressed by means of a ratio that will have the following form for each one of the three kinds of prices:

$$TPAC = 1/n \sum_{t=1}^{n} \left(\frac{TCPI_t}{GCPI_t}\right)$$

$$NTPAC = 1/n \sum_{t=1}^{n} \left(\frac{NTCPI_t}{GCPI_t}\right)$$

$$IPAC = 1/n \sum_{t=1}^{n} \left(\frac{GCPI_t}{ICPI_t}\right)$$

Where: "TPAC" is the alignment coefficient of tradable goods inflation to general CPI, NTPAC is the alignment coefficient of the non-tradable inflation to general CPI, and IPAC is the alignment coefficient of the general CPI to an International Consumer Prices Index relevant to Chilean foreign trade.[155] In the long run, in open economies such as the Chilean one, it would be plausible to expect a similar tendency (or range of evolution) in the price progression of each product that made up part of the same basket by which CPI is estimated.

However, if one or more industries have the capacity to maintain the evolution of their prices over the price evolution of general CPI, some factor is allowing them to do so. The PAC permits the identification of the behaviour of relative prices facilitated by conditions of the competition of industries and markets.

The same applies to the relationship to be established between the CPI of the Chilean economy (strongly conditioned by the relative weight of TCPI and NTCPI) in relation to the international inflation relevant for the country as a whole and reflected through behaviour of IPAC. All these tendencies of pricing behaviour can be determined through numerical estimation of the PAC and comparison in time of two or more observations of this index; then depending upon the values of those estimations, we would have the following basic options:

> **PAC t n < 1**: which means that industry has no (or does not put into practise) any market power. That show an industry whose company's lack of capacity to maintain the ratio of indexes (Px/Py) over the ratio of indexes built on weighted

155 The methodology and figures used to estimate three PAC are reported in a detailed way in Appendix II. The construction of an international CPI that includes prices relevant to the Chilean economy is specifically detailed.

average prices of the products that are included in the CPI basket during the observed period.
PAC t n > 1: which means that the industry has (and has exercised) some market power; we would show one industry that would have the capacity to maintain high ratio of indexes (Px/Py).

If we compare two moments of an interval of time (e.g. 1990–2009) the CAP might be associated with one of three possible scenarios for a particular branch or industry:

PAC t1 > PAC tn: Shows a deflation of prices as a result of a competitive context, which means a trend towards the increasingly competitive behaviour of an economy or industry.
PAC t1 < PAC tn: Shows a price raise as a result of the significant market power of the companies that are gaining market power with respect to the other companies whose products are included in the basket of the CPI.
PAC t1 = PAC tn: Shows a situation in which there is a structural alignment of prices between the industries being compared.

These coefficients, as well as providing an order of magnitude of the market powers, can be used to infer changes in the structural characteristics of the markets through inter-temporal comparisons. The estimation of the respective PAC gives us the following alignment tendencies reported in Figure 5.4.

Then:

$TPAC_{1990-2009} = 0.88 < 1$
$NTPAC_{1990-2009} = 1.11 > 1$
$Inter\ PAC_{1990-2009} = 1.24 > 1$

Given the TPAC´s $_{1990-2009}$ values, we can conclude that the tradable products industry has no relevant market power.

Given the NTPAC´s $_{1990-2009}$ values, we can conclude that the non-tradable products industry has a relevant market power.

Given the international PAC´s $_{1990-2009}$ values, we can also conclude that in the Chilean economy as a whole, there are some industries of high market power and critical

relevance within CPI basket, generating a growing misalignment between domestic and international inflation.

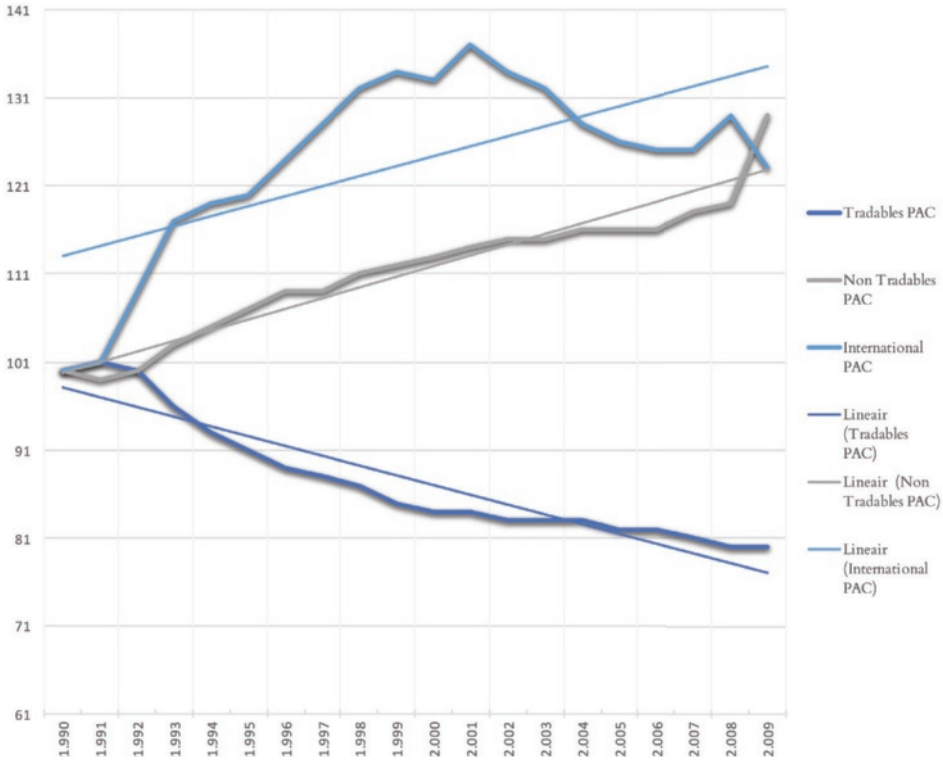

Figure 5.4. Evolution of Coefficients of Price´s Alignment in Chilean Economy
Source: Author´s elaboration based on INE prices´ data base.

Those industries would be exercising their power in such a way that general CPI is highly influenced by them and given the gap among values of the TPAC and NTPAC, it is sound to think that such industries would be placed at the sectors that produce non-tradable goods. From the table attached to Figure 5.4, it is clear that between 1990 and 2009, the TPAC tended to decrease and the NTPAC tended to increase. For its part the IPAC, although it exhibits a period of growth followed by another of weakening, in general it maintains a clear upward tendency as displayed by the linear trend. Both periods are explained by the influence of the TCPI/NTCPI relationship, which shows the sustained presence of a gap between the evolutions of these two components of the GCPI.

Only between 1990 and 1992 did prices of tradable goods grow at higher rates than non-tradable goods did; from that year onwards, the tendency has been the opposite. In 2009, whilst the tradable goods recorded inflation of 4.92%, non-tradable goods registered an inflation of 7.44%, i.e. a degree of difference of 2.52% between the increase in the prices of tradable and non-tradable goods. This price differential directly affects the GCPI between its evolution and the evolution of the NTPAC, throughout the period under analysis. It registered a significant difference (47%) as domestic inflation rose at rates of 5.5% per year whilst the international inflation relevant to Chile did so only at rates of 4.6% annually.

If we analyse this tendency in more detail, from one side it is clear that this gap is explained by the fact that, even though TCPI (clearly influenced by trade openness) was only 4.92%, 7.44% was registered by NTCPI (more influenced by domestic factors). NTCPI clearly overhauled the impact of tradable goods prices producing a significant price misalignment, given that Chilean CPI is almost 20% higher than ICPI.

From the other side, we observe that the NTCPI is 51.2% bigger than TCPI. This information suggests the presence of a regular non-tradable goods mark-up triggered by the considerable market power of large companies operating in that sector. This market power allows them to transfer fluctuations in international prices to domestic currency without diminishing their profits, as well as setting the market prices of their products consistently above domestic cost.

The opposite happens with the TCPI evolution, which corresponds to the inability of tradable goods producers to transfer the increase in international cost to domestic prices, because the tradable goods sector has no greater market power that its companies, as a result of trade openness, are facing high levels of competition both in domestic as in international markets that does not allowed them increase their prices discretionally.

The generation of the aforementioned market powers does not seem to be due to an incomplete opening of the economy; the Chilean economy is fully open. In our opinion, the current oligopolistic structure of Chilean markets is a direct consequence of a trade openness carried out in an institutional context characterised by markets that had a strongly oligopolistic organisation before their opening (Lagos, 1962; Pinto, 1973; Hurtado et al, 2008) but which openness deepened and nor supress as neoliberal promised.

Within the process started by the dictatorship and reinforced during the post dictatorship governments, the bulk of state-owned enterprises that operated in monopolistic or oligopolistic markets were transferred to some business groups, setting permissive regulatory frameworks and antitrust institutions of dubious effectiveness and strengthening prevalent non-competitive market structures. This fact expanded and not reduced oligopolistic Chilean market´s structures.

However, another factor must be added as explainable variable of concentration. Chile is a small economy with small markets. For that reason and given the nonexistence of an explicit institutional effort to build new markets arrangements for promoting competition, the trade openness had tended to reinforce trends towards concentration already present before trade openness and have continued doing so after.[156] Nonetheless, after trade liberalisation all these factors were reinforced to an extreme degree by the presence of antitrust institutions lacking of real power and competencies and by the presence of an institutional environment that allowed the emergence of a large number of institutional arrangements, which enforced economic concentration.

Some aspects and characteristics of the Chilean oligopolistic market structure was certainly installed before trade openness, but during the setting up of the Chilean model, the neoliberal promise was that opening and market liberalisation would eliminate the oligopolistic powers present in local markets, in a radical way. Given that it was the original promise, we consider it a crucial point of reference against which the outcomes of trade openness should be judged.

The neoliberal promise of "more competitive markets" does not seem to have been fulfilled at all. If we can find evidence of higher and rising degrees of market competitiveness in the Chilean economy 1990-2009, the whole path of trade openness and market liberalisation would be entirely justified. However, during our research, it was not possible to find that evidence; the performance of the Chilean economy seems to contradict, rather than confirm, the optimistic neoclassical and neoliberal view,

156 The bulk of developing countries are characterised by similar conditions to Chile, e.g. small markets and highly oligopolistic and weak antitrust institutions. Therefore, the effect of those conditions in a context of economic openness should not be too different from that which occurred in Chile. The impact of neoliberal policies in countries with larger market sizes, such as Brazil and Mexico, was not too different. That is a fact that suggests that economies of scale related to the size of the markets have played a role similar to the barriers to entry that generates oligopolies operating in small markets. However, demonstrating this hypothesis exceeds the scope of this research.

which predicted two direct effects of trade openness: alignment of domestic prices to international price and a greater competition in domestic markets.

5.5. Which Factors Explain the Misalignment of Domestic Prices?

The neoliberal thinking tends to attribute evolution of the real variables to the influence of monetary phenomena. In an open economy like Chile; they assume that RER should be associated to the ratio between the domestic and international prices, measured by means of the ratio of tradable and non-tradable CPI (TCPI/NTCPI). In this way, RER should evolve along with this ratio, evolution of the prices of tradable and non-tradable would keep a consistent trend, will also do so the real exchange rate and therefore the relationship between the evolution of exports and imports will follow a predictable path, which should push down domestic inflation.

From there, they try to explain theoretically why the evolution of consumer spending patterns, induced by new relative prices, can affect the evolution of Real Exchange Rate (RER) and validate the law of one price (Johnson, 1972). Accordingly, a more open economy will increase the percentage of the aggregate demand which should be spent on tradable products (Blanchard and Jeffrey (2009:404)) and hence the share of tradable goods in the economy (e.g. imported inputs for tradable and non-tradable sectors and consumption of imported tradable goods).

The same can be postulated in a different way: the more open the economy, the less relevance that the non-tradable sector should have. However, in the real world this is only one aspect of the total openness effect.

The impact of the relationship expenditure/GDP (measured at current prices) on RER should also produce an increase in the total expenditure of the economy (public and private). This, ceteris paribus the GDP level, can manifest in a growing demand for non-tradable products. If Chilean demand for non-tradable goods is greater that the demand for tradable goods, it would result in new demand patterns associated with growing prices of non-tradable products,[157] with the subsequent fall of the TCR (the so-called Salter-Swan effect).

157 Greater demand for non-tradable goods is resulting from the increase of per capita income of the economy and higher demand for tradable goods is resulting from the lower prices induced by the trade openness.

If we look again the results of Figure 5.3. A, the Salter-Swan effect seems to apply to the Chilean case, insofar as the RER (first line from below, X marked) evolves in a way that closely follows the relationship of prices between tradable and non-tradable (second line from below). In the period studied, the TCR fell steadily, as did the ratio (TCPI/NTCPI, ◊ marked). It is worth stating that in the Figure 5.3 B the price of non-tradable (the superior line, ‡ marked) rose more strongly than tradable product´s prices (inferior line, ◊ marked) increases the distance among two indexes, parallel to appreciation of Chilean currency value.

From Figures 5.3-A and 5.3-B, it is also possible to see that the differentiation process between price evolution of tradable and non-tradable does not look be correlated with evolution of the real exchange rate (RER). That rate, which for more than twenty years has maintained a nearly constant trend, has been evolving around an average level close to eighty per cent of the base year 1990 =100.

The neoliberal hypothesis (that uses as its claim the presence of the Salter-Swan effect) holds that, in the Chilean case, absolute growth of income and of expenditure would be the variables that operate in favour of the higher increase of NTCPI. This argument neglects the low price-elasticity of demand that characterises the non-tradable sector and over-emphasises the impact of incomes growth on the variations of prices.

In the Chilean economy, this view considers that changes in relative prices shaped a system of incentives that expanded productivity in the tradable goods sector, while non-tradable goods prices originally remained constant. Nevertheless, when GDP per capita and the marginal cost of production increase, non-tradable would also increase in price. Additionally, from a neoclassical view (not necessarily neoliberal), it is assumed that a second effect is present which takes place when GDP rises. In this case, the new income level will influence demand for non-tradable products generating a further increase of the NTCPI, now originated by the GDP growth. Based mainly on this situation, both approaches (neoliberal and neoclassical) maintain that the law of one price is only applicable to the tradable goods, as much the non-tradable goods define their price level from the interaction of supply and demand (Dornbusch, 1982).[158]

158 Theoretically speaking, in an open economy immersed into international competition and increasingly next to the neoclassical conditions associated with perfect competition (but without international labour mobility), the marginal costs of production of tradable products, plus their transportation costs, must tend to equalise marginal income of consumers at some level of prices characteristic of a competitive market. For that reason, a mechanics of market adjustment takes for

From Chilean economics mainstream, the impact of GDP per capita growth over tradable and non-tradable price evolution is generally analysed in a way isolated from different modalities of markets competition existing in each economic sector and neglecting differential applicability of the law of one price.[159] In spite of this assessments, it is well know that, although the higher levels of external competition predominating in the Chilean economy, the supply of tradable products as well as the demand for these, tends to be more elastic than demand in the non-tradable sector, characterised by low competition. Different frameworks induce clearly different behaviours in the economic actors of one and another sector.[160]

In sum, at the base of the neoclassical and neoliberal approaches is the assumption that, in Chile, the impact of income´s demand elasticity of non-tradable goods is bigger than impact of price´s elasticity of demand of those products. For that reason,

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granted that in the long term, prices have some degree of "flexibility". These kinds of prices are identified as "efficient-prices" or "shadow prices". If the market price of a product is approaching its price shadow, it means that each additional unit of consumption would be as valuable as any additional investment units. That assuming that the marginal utility of an additional unit of consumption would not change with the level of income of the receiver. In practical terms, in that context, when neoclassical theory accepts that prices of products equal their marginal costs, and that inter-country wage differences in the sector of tradable products correspond to productivity differentials, if technical progress in the non-tradable sector is faster than in the tradable sector, then non-tradable inflation will be larger than tradable product inflation (Balassa, 1964). This theoretical hypothesis is built on very restricted assumptions, however has been used frequently by neoliberal economists in order to discourage any policy intervention in a different direction than that being indicated by market forces.

159 From the neoliberal point of view, the non-applicability of the law of one price to non-tradable sector must be considered a frictional situation. From their perspective, a higher income growth and a rising incorporation of tradable input in non-tradable goods should induce, in the long run, the alignment of domestic tradable prices to the international prices of similar goods.

160 De Gregorio (1984) found for aggregate imports, a price elasticity of - 0.47 and an income elasticity of 2.2. When he disaggregated price elasticity of imports, noting that consumer goods were those who had higher elastic price and income, he concluded that imports of capital goods and intermediate goods were insensitive to variations in prices. In the case of exports, he found that the price elasticity of exports takes values between 0.2 and 0.3 in the short term and between 1.0 and 1.6 for the long term. In addition, he calculated the elasticity income with respect to the level of world activity, which turns out to be 0.2 in the short term and between 0.9 and 1 l in the long term. Using panel data, Saenz and Lobos (2011) estimated that the price elasticity of demand for interurban motorways in Chile was generally inelastic to the toll. Agostini, Plotter et al (2011) estimated that for residential consumption of electricity there is price elasticity between - 0.38 and - 0.40 and elasticity income of between 0.11 and 0.12, depending on if they are evaluated using the median or the mean of the independent variables. About water price elasticity, there are numerous international studies showing high inelasticity of the residential water demand. (Espey et al, 1997; Klaiber, Smith, et. al., 2012).

NTCPI´s climb is visualised because of a greater GDP per capita and not because the low demand elasticity existing in the market of non-tradable products.

However, there is numerous evidence which contradicts this point of view, even taking into account the multitude of products and periods in which these results are estimated or the poor quality of available data, which makes interpretation difficult in some cases. If we observe the evolution of the Nominal Exchange Rate (NER) of the Chilean economy (Figure 5.3-A, **+** marked)), it appears that changes in inflation rates (whose average is higher than the nominal exchange rate) are not being adequately transferred by means of the pass-through effect of NER´s fluctuations.

Given that we previously observed that the CPI growth heavily exceeds the rising labour costs and we now observe that they also surpass nominal devaluations, we would have already accumulated two variables that seem to possess a low level of explanatory capacity of deviations of the relative price level. This would suggest, without a yet defined causal relationship, that inflationary pressure is probably related to other factors. For that reason, we will concentrate on variables different to exchange rate and labour costs, focusing our exploration specifically on the market's organisation.

There seems to be a big difficulty in assuming the neoliberal claim which assumes that the degree of trade openness will generate an automatic transmission of changes in relative prices; if domestic prices are not "efficient-prices", the obvious conclusion is that neoliberalism expects too much from trade openness in terms of price alignment, and without that alignment it would be very irrational to wait for productivity improvements and efficient resource allocation.

Given that, we will try to prove, based on the information gathered in our research, that the Chilean situation operates in a quite different way than neoclassical-neoliberal forecasts, related to construction of a system of efficiency prices. In fact, we will show that the progression of events in the real economy has been quite different from the predictions of mainstream analyses.

In the Chilean context, it seems relatively clear that the bigger impact of trade openness in GDP has been caused only in a low degree by changes in local relative prices that would have reallocated production factors from inefficient sectors towards the most efficient. Instead, the large positive effect of exports seems to obey variations in the absolute price of commodities exported by Chile, especially in the price of copper,

which has produced a major economic growth. That dynamic has been induced from the large-scale copper mining. A sector in which foreign investment has increased almost 9-fold between 1990-2009, reaching almost US $14,000 million annually (Meller, 2013). The impact of these investment volumes and the increasing weight of the large copper mining sector, have impacted all of Chilean exports. However, these results essentially show the impact of the mining sector and cannot be attributed to the performance of the tradable sector as a whole. Neither does the available data show that the effect in the relative prices of the economy are the variable that drives the export sector (60% concentrated in mining exports), nor does direct foreign investment (which is 50% oriented to the great copper mining) seem to be determined by local relative prices.

The Chilean GDP increase occurred within a dynamic without regard for the resource reallocation process. The paradox of the situation is that the opening has not been associated with the higher levels of competition in the domestic markets, or the allocation effects that this should produce.

Moreover, the negative effects of the lack of competition in the Chilean markets have been somehow obscured by the impact that the already described copper mining investments have had on the economy. It is not the same to asses that trade openness exerts a reduction of prices of some manufactured goods (before produced domestically and now imported and merchandized by large trade firms) which assume that at the present time, as a result of trade openness, international prices are exerting an impact in the relative domestic prices, in such a way that it is bringing a better and comprehensive allocation of resources in the economy as a whole.

When in an economy there is some level of competition among or within tradable and non-tradable sectors, that circumstance influences the tradable pricing strategy (e.g. in the short term the suppliers of tradable products will tend to develop pricing strategies in local currency to avoid the loss of market share (Bacchetta and Van Wincoop, 2002). Then, at a lower level of competition the price elasticity of demand will be less, and the market power of dominant firms that strongly control price behaviour will be higher. That circumstance, at first sight, seems to be associated with a worse allocation of resources and not with a better one; nevertheless, before we extract more conclusions, we think that it is necessary to complete the appropriate characterization of the trade openness on the relative prices of the Chilean economy and about the influence that relative prices exert on the levels of competition existing in the markets.

5.6. The Price Transmission Effect After Trade Openness

Chile is a small open economy in which, supported by neoliberal institutions, a smaller number of companies have been able to take control of the supply of goods on the domestic markets of non-tradable goods and services. From 1973 forward, in Chile installed an institutional environment that fostered economic concentration, building important market power differentials between companies, reinforcing this context lacking of serious market competition. Is due to the presence of that context which, we can plausibly explain the dynamic of relationships among tradable and non-tradable prices and also the price´s pass-through effects.

At the academic literature, the explanations of the relationship between a full openness and a low pass trough are diverse. For example, Yang (1997) argues that the degrees of pass-through are positively correlated to product differentiation and negatively to the elasticity of marginal cost; Campa and Goldberg (2005) reported that changes in the composition of imports bundles in favour of manufactured products, helps to explain the decrease in the NER pass-through. In addition, Marazzi and Sheets (2007) found that part of the reduction of the pass-through of the exchange rate on prices of imports into the United States is due to low prices of imports goods from China. Daniels, Mazumder et al (2015) find a negative and significant relationship between openness and the cost of lost production in relation to the percentage change in inflation ("sacrifice-ratio"), regardless of the transmission channel that is proposed.

Nevertheless, all these theoretical approaches, remain a core question which requires empirical answers: why does pass-through of international prices not cause a large impact of international prices in the Chilean economy (i.e. lower inflation or larger deflation) regardless of full trade openness?

That situation represents an issue very difficult to explain from the neoclassical point of view and even more so if you try to explain it from the neoliberal perspective, which assumes that a combination of growth and opening would produce lower prices of tradable goods and higher prices of non-tradable goods. Based inter alia on higher GDP and increasing labour costs.
In spite of this view, in Chile all evidence shows that wage pressures are exerted in the labour market as a whole (i.e. tradable and non-tradable sectors) and more than that,

they are higher in tradable sector than in non-tradable sector (DIRECON, 2009:4).[161] For this reason, it is clear that assumptions about the presence of bigger wage pressures at the non-tradable sector as explanation of rising prices are not supported by empirical evidence.[162] On the contrary, the fact that in Chile 1990-2009, tradable prices raised less than non-tradable prices it is eventually explained by the contribution of at least two factors, others than wage pressures and exchange rate influence: In the first place, firms producing tradables and non-tradables will try to reduce the impact of rising wages on their costs, increasing the prices of their goods or services; but obviously, the success of such a strategy is not a function of the owners´ business will, but the price elasticity of demand that they will face.

Given this, the result of that rising nominal wages may produce two different consequences: A higher level of inflation or a lesser level of sectorial profits, all depending significantly on the characteristics of demand. Secondly, if technical progress associated with the trade openness process could be absorbed more quickly in the tradable than the non-tradable sector, this would be a reasonable explanation for the higher increase of prices in the non-tradable sector.

In fact, worldwide productivity has been growing much more in the tradable sector and evidence shows that this last behaviour seems to fit adequately in the Chilean case (De Gregorio, 2007:245-46).[163] However, those tradable sectors have a production that is highly intensive in utilization of non-tradable domestic inputs (Alvarez, 2004), Chile´s competitive advantages are based firstly on cheaper domestic inputs (labour and natural resources) and secondly on low cost imported technology. However,

161 In Chile, total mass of wages in export business is roughly equal to 32% of the mass of wages in the country. Export companies have been increasing wages and for that reason, these are higher than the average country wage. Companies with shipments abroad (i.e. companies that sell both the domestic market and the external market) represent less than 1% of the total number of companies in the country, but create employment for 17.3% of the country workforce" (DIRECON, op. cit., page 4).

162 We should remember that analysing the behaviour of global inflation and non-tradable, Gregorio et al (1994:1243) observe the simultaneous presence of low inflation and increase in the price of non-tradables for country members of the OECD, a behaviour more similar to predictions by neoclassical theory than behaviour shown by Chile, in which both variables move in the same direction.

163 There are many empirical evidences that in Chile, mayor technical improvements can be seen in the tradable sector (i.e. cooper, wine, fresh fruit, salmon and cellulose). A good proof of the bigger technical progress of the tradable sector is the significant appreciation of Chilean currency, since when a country grows technologically more than the rest of the world, its exchange rate decreases to the extent that such technical progress is greater in their tradable goods sector.

the technology that is imported by Chilean firms is not of the first line, but they are "balances of previous seasons" left behind by the countries that provide it, due to the strong weight that the investments in innovation have in them. Given this, it is unlikely that the country will be able to build solid competitive advantages that will allow it to deal in the international arena.

On the other hand, the non-tradable sector is highly intensive in the use of tradable goods used as inputs. Both elements should tend to equalize national and international prices and tradable and non-tradable should present lower prices increases, especially in tradable sector. Nevertheless, reality has been evolving in a different way, a fact that confirm the difficulty of neoliberal analysis to elucidate why differential prices between the domestic and international inflation subsist and it is amplifying.[164]

Neoliberal analysis must be characterized by its lack of focus on the high market power of the firms located on the non-tradable sector and by the insistence in the presence, as a key factor, of pressures of costs faced by firms. However, actually low sectorial cost pressures seem to predominate on the non-tradable sector[165] given the simple fact that, in domestic markets, non-tradable producers are obtaining cheap inputs from the tradable sector. The non-tradable products also confront a very inelastic demand due to the lack of foreign competition and by the strong market concentration; this context widely reduces the possibilities of consumption´s substitution and possibilities to widen mark-up.

The origins of quoted price differentials cannot be placed on the area of exchange rates. Rather, it seems that adjustments of the nominal exchange rate are a consequence and not a cause of the Chilean inflation. Inflation pressures coming from the non-

164 The Chilean imported goods that have a greater weighting in the CPI basket include automobiles and gasoline, relevant products given that Chile is the only Latin American country that has no oil. Also important are several types of meats, which are both imported and exported, electrical appliances, and high technology products, of which very few are produced in Chile after the dismantlement of such industry following trade liberalisation. Other tradable products, both imported and exported, are textiles, clothes, soaps and detergents, pet food, some pharmaceuticals and tourist packages.

165 This situation is confirmed by the analyses carried out from inside the IMF. (Cuddington, Ludema and Jayasuriya (2007); Cuddington and Jerrett (2008); even this new trend of commodity prices (that increases prices and incorporates imported inputs more and more cheaply) has only been associated with the definitive failure of the ideas of the structuralism of ECLAC by the IMF authors, which sustain that technical progress in manufacturing tended to reduce the use of raw materials and energy thereby causing demand for primary products to grow slower than demand for high technology goods

tradable sector must be explained by the fact that the effects of devaluation in this sector can be fully transmitted to domestic prices (and even surpassed, depending of future inflation´s expectations) and the effects of revaluation are not necessarily fully transferred. Both factors only become possible given the high market power of large firms operating in the non-tradable sector.

If the relative prices are one of the major determinants of the capital-labour ratio to be used by an economy, when these prices are distorted by the weak market competition, it is difficult that the distorted prices do not exert a negative allocative influence (Dwyer, 1992). The way in which firms combine factors of production to produce goods and make profits depends largely on input prices. On the other hand, output prices depend very much upon the business decisions made regarding the function of relative prices of both kinds of goods.

In Chile, as in most NDE, the relative cost of production of the tradable and non-tradable goods sectors is an extremely important variable in defining the price levels, in the same way than in all open economies. However, if prices installed by trade openness are not really efficiency prices, it would be very difficult to obtain efficient resource allocation and productivity improvements associated with trade openness.

In terms of Chilean inflation, there no other option to recognise that there are relevant allocative problems related to non-competition structures prevalent in this economy. If after almost 40 years of trade openness, domestic and international prices remain misaligned, this means that they are not transmitting the appropriate signals to the process of resource allocation, and in some way inflation is highly influenced by the presence of a resource misallocation problem. For this reason, the neoliberal hypothesis of a better allocation of resources based on the alignment of domestic and international prices, actually seems to lack empirical validity.

The situation that we have analysed in this chapter has shown us, in a categorical way, that:

1. Chilean inflation is clearly higher than its major trading partners,
2. The presence and maintenance of mark-up of prices is more than evident in the main markets of goods and services.
3. National relative prices are clearly out of line with the prices of their global peers.

4. The price relationship between tradable and non-tradable products, seem to depend on the market power of the companies that are part of one or the other sector, and not on the new relative prices induced by the trade openness, which are severely misaligned.

Using the data showed in this chapter, even if we do not use an economic analysis of greater quantitative sophistication, there should not be too many doubts that a price system grounded upon these four characteristics can hardly be constituted by "correct prices". Neither, can it be assumed that the new and misaligned relative prices of economy will be able to generate a new and efficient allocation of resources.

The available data certainly seems to confirm this vision, which is otherwise very similar to those outlined in theoretical works by Krugman (1986), Dornbusch (1987) and Menon (1996), who posited that imperfect competition market structures present an incomplete transmission effect. In fact, Chile´s economy seems to fit with some market situations in which the prices are higher than the marginal costs and producers can obtain profits greater than zero. This remains independent of the fact that the economy is operating, in the long term, on international markets with high levels of competition. From that perspective, the ways in which the mark-up responds to variations in the international prices depends on the number of companies operating in the market, more than it does NER. The segmentation existing in the market (a reality which can limit the arbitrage), would depend on the degree of product differentiation and on the functional form of the demand curve.

In economies, similar to Chile and in Chile itself, as we will later analyse, it is possible to assume that a cause for the incomplete pass-through of the exchange rate is the presence of price management mechanisms based on market powers highly impermeable to openness. As such, firms can adjust mark-ups in order to absorb part of the movements of the exchange rate (Adolfson, 2001); thus, the outcome will be a greater level of pricing that is not based on a high competition framework associated with a smaller pass-through.[166]

166 Authors like Taylor (2000) maintain that in a context characterised by oligopolistic market structures, domestic prices will behave with relative independence from the trajectory of the nominal exchange rate. In the same conceptual line, Goldberg and Knetter (1997) and Burstein, Eichenbaum et al (2003), found that even in the context of open economies, the presence of final products that embody non-tradable inputs determines that the transfer of exchange rate to prices is incomplete.

In the Chilean case, we can observe the significant market power of large-scale firms. If those enterprises provide input to production of non-tradable and tradable goods, that power will impact the CPI as a whole. Thus, when exchange rate volatility increases, there will be several reasons for companies to use their market power to set prices using the value of foreign currency and so not absorbing the magnitude of the changes in the nominal exchange rate, transferring it to prices. Additionally, there will be incentives to price their products in the local currency, adding an increasing mark-up.

In this context, the magnitude of the transfer from nominal exchange rate to prices is endogenous and depends on the structure of the local market, as well as on the degree of the nominal exchange rate´s volatility, a variable that conditions inflation expectation. For that reason, Chilean wholesale prices seem to be less sensitive to exchange rate variations than import prices, explaining the existence in the distribution chains of a less than perfect pass-through[167].

In agreement with the above, low levels of competition in Chilean markets seem to be determining the high level of inflation recorded by the Chilean economy in relation to its major trading partners. It also determines its low alignment to international relative prices and hence the low capacity of it to properly allocate the resources of the economy. The poor ability to transfer price signals coming from abroad to domestic markets would explain the low pass-through the economy, as well as the excessive price inflation, which Chile presents in its non-tradable goods sector and the economy as a whole.

The evolutionary trends previously analysed seems to indicate that the lack of competition in the markets is the main limit to the Chilean economy behaving according to the neoliberal promises made subsequent to trade openness and the installation of a new system of relative prices. Moreover, as we will discuss in this chapter, it appears that the implementation of the neoliberal agenda is what has fostered the presence of institutional arrangements producing a subsequent lack of competition.

167 We have not developed our own estimation of the pass-through of the Chilean economy, since these are abundant studies on this issue. But it is be useful to remember that Chilean pass-through was estimated at levels that fall from 0.17 a 0.04, in the short term, and from 0.48 to 0.11, in the long term (Edwards, 2006; Mishkin y Schmidt-Hebbel, 2007).

5.7. Liberalization provoke improvement on market´s competition?

If the basic forecasts associated with the implementation of the Chilean Model would have proven to be correct (i.e. that free and open markets would create by themselves a system of relative prices that would efficiently allocate the resources of the economy towards disseminating technical progress), fully assuring a country's path towards development. But, if those had been the actual results of a trade openness, Chile should already be a developed country (at least as much as Portugal is) since it has opened and liberalised its markets more drastically than almost any other country. However, we must first remember that the validity of these assumptions depends not only on the insertion of this country in competitive global markets but, above all, upon the level of competition existing within its domestic markets and the impact of this on the efficient allocation of resources of the economy. Secondly, it is necessary to stress that competition levels depend on the specific institutional arrangements that characterize these markets.

The neoclassical theory assumes that, even from a domestic situation in which some specific arrangements produce that non-competitive markets predominate, trade openness will finally destroy market powers through price arbitrage, in such a way that, in the medium and long-term, markets would become highly competitive. In that context, the economy will amalgamate in progressive ways, new institutional arrangements which consolidate competition, free mobility of economic resources and also will reduce at minimum market powers and oligopolistic market structures (Carlton, 1994, 137-8).

As is well known, "market power" is the ability of companies to set prices higher than those that would exist in a context of competition, so that the market prices of products (P) exceeds their marginal cost of production (MC). Thenceforth, in the general case for any non-competitive market, if a product has:

$$\mathbf{MC < P} \qquad \textit{it would imply that:}$$

$$\mathbf{P = (MC + \phi)}$$

The term ϕ would be a margin determined at the company's discretion, which would constitute a surplus earned by capital over cost of production or, expressed in another

way, a "mark-up" or extra-charge, characteristic of a context of imperfect competition. The effects of competition and trade policies on a company's market power are typically measured through such mark-ups (De Loacker and Kaczynski, 2012).

Within the neoclassical hypothesis, when companies succeed in maintaining these non-competitive benefits during some period of time, such a situation can generally be explained by the presence of entry barriers (technological, economic, or legal) or by the presence of collusive arrangements. A specific cost-price relationship is the formal condition that usually defines to imperfect competition in the long term (Robinson, 1973). Within this relationship, the difference between P and MC would be the previously referred mark-up (**ϕ**) which may be expressed in the following way:

$$\textbf{(1)} \qquad \Phi_c = \frac{P - MC}{MC}$$

This is equivalent to assuming that the "mark-up of costs" is the difference between price and marginal cost, measured as a proportion of the marginal cost.[168]

The equation **(1)** could also be expressed in the following way:

$$\textbf{(2)} \qquad MC = P / (1 + \phi_c)$$

From the equation **(2), it** could be argued that in a non-competitive market, the marginal cost of a product would be tantamount to the market price discounted by the value of the mark-up. However, if we assume the presence of a situation of perfect competition, then prices, marginal cost and marginal revenue (MR) become equal. Then, using the standard definition of the marginal revenue, in which the coefficient "ε" corresponds to the price elasticity of demand we have:

168 While the demand for its product faced by a company is not infinitely elastic, there will be a margin over the marginal cost called "mark up of costs" (ϕ_c) expressed in equation. (1), which is estimated as the proportion representing the differential between price and marginal cost (regarding the marginal cost). On the other hand, the "mark up of prices" is the ratio that represents the differential between price of a good and its marginal cost (regarding the price). The mark-up of prices (ϕ_p) can be expressed by means of a ratio that is named the Lerner index (L), which is the negative inverse of price´s elasticity of demand, meaning the value of the relationship existing between the prices which an industry charges for its products and the demand in the market (**L= −1/**ε). In such a way, the index describes the relationship between price and price elasticity of demand and the limits that price elasticity imposes on the pricing process of those companies seeking to maximize their benefit beyond the boundaries of perfect competition.

$$(3)\ MR = P\ (1 + 1 / \varepsilon)$$

The equalisation between marginal cost and marginal revenue (2) and (3) could then be expressed in the following way:

$$(4)\ P / (1 + \phi) = P\ (1 + 1 / \varepsilon)$$

with some arrangements, we have:

$$(5)\ \phi_c = 1 / (1 + \varepsilon)$$

Equation (5) represents the relationship between cost mark-up ϕ_c and price elasticity of demand ε, from there we can conclude that to lower values of elasticity, a greater proportion of price is liable to be charged as mark-up. In view of the fact that companies are looking for the maximisation of its benefits, they will act on the elastic portion of its demand curve only if they cannot avoid it. This implies the presence of a negative relationship between elasticity of demand for their products and the market power that they have in that market.

Therefore, in the area that we are concerned with, the more important issue to be analysed will be the way in which, in a context of trade liberalisation, factors correlated to demand inelasticity may limit the alignment between internal and external prices and hence induce serious restrictions on the process of efficient resources allocation forecast by neoliberal discourse.

If the demand elasticity is defined from the specific institutional arrangements that determine the actual sensibility that demand has to price changes, the question to answer would be:

> In which measure do the influence of these arrangements counterweigh or eliminate the impact exerted by the change in relative prices?

Answering this question presents some complexities. As we said before, market power enforces the ability of companies to arrange selling prices above the marginal cost of each unit, i.e. a situation in which the mark-up of costs is positive ($\phi_c > 0$) and that is only possible in markets where competition is imperfect. In a way, analogous to the derivation of cost mark-up ($\phi_{c)}$ in equation five, the price´s mark-up (ϕ_p) can be

derived. The difference between P and MC may also be expressed as a proportion of the price (P-MC/P). That expression that is commonly called the Lerner Index (1 /-$\mathcal{E}$), is the reciprocal of the price elasticity of the demand.

In our case, estimation of market power is a key variable to understand the specific way in which market governance was built. In an open economy, prices are the key variable that defines institutional arrangements. If a small group of firms concentrate a high market power, they will have a high decision power in relation to any other firm which, acting as a price taker, make part of a chain or economic sector. The arrangements among economic actors are mostly defined by the relative power of each one of them; as a consequence, chain governance will be also a by-product of the unequal actor´s market power in a context of non-perfect competition.

Measuring the presence of eventual concentration requires a specialised tool like the Hirschman-Herfindhal Index (HHI), which is a measurement commonly used to establish the level of competition that exists within a market or industry.

$$(6) HHI = \sum_{i=1}^{n} Si^2$$

This index gives an indication of how the distribution of market share occurs across the companies included in the index. It acts as an indicator of market structures, since it takes into account both the number of competitors and their relative participation in the market, and is calculated as the sum to the square of the percentage participation of the i-th company in the industry. Where "Si" is the percentage of market participation of i-th Company in the market and "n" is the number of companies within the industry, sector or group of companies used in the analysis.

To understand how market power operates in this area, lets us formally demonstrate how oligopolistic markets operate. They must satisfy the following condition:

$$(7) \quad \sum_{i=1}^{n} S_i^2 * \frac{P - MC}{MC} = \frac{HHI}{|\mathcal{E}|}$$

That means that the level of a firm's market power can be expressed by relating price to marginal costs. The difference between price and marginal cost is expressed as a percentage of prices, being equal to the reciprocal of the price elasticity of market demand. In other words, this means the square of the market share of each company ($\sum si^2$) multiplied by mark-up of price equal to the HHI, divided by the price elasticity of demand. Then, in the previous equality (7), the condition that must be present is that if the price elasticity decreases, the market power rises. Then we can conclude that a positive relationship exists between market power and the degree of concentration measured by the HHI.

This means that if we have the HHI and the elasticity of demand, we can calculate market power. This fact is important because the marginal cost of production is more difficult to estimate than the HHI and the elasticity of demand. For this reason, the HHI is an indicator of the market power of companies, which lets us establish a relationship between concentration and price elasticity of demand for Cournot models, relating it to the Lerner index (L).

Using HHI assumes a paradigm that relates structure, conduct and performance (Christakis and Bausch, 2006), we are accepting the presence of a sequential relationship between structure (concentration), conduct (pricing) and performance (market power). This approach focuses on structural influences on conduct and on the way in which both of these factors influence performance.

The relationship established between market structure and a firm´s conduct indicates that collusion is easier amongst a small number of firms, and the relationship between conduct and performance implies that the more competitively firms behave, the smaller their market power and the higher their allocative efficiency. However, there are alternative hypotheses, whose validity needs to be analysed before accepting as useful the paradigm that suggests that, in the Chilean economy, the simultaneous presence of concentration and allocative in-efficiency phenomena form a cause-effect relationship.

In this regard, we can emphasise that market power does not depend only on demand elasticity. The level of market concentration and the degree and type of collusion also exert important effects. If the behaviours of the incumbent companies and those of the defiant ones in each market are separated, assuming that the incumbents are positioned closer to the technological frontier, they could survive innovating.

On the other hand, non-incumbents, located much further away from that border, will be in a more difficult position if they want to compete based on innovations, especially when the economy opens up to international trade and all sizes of companies face greater competitive challenges (Aghion and Griffith; 2005). In other words, the institutional environment (the big rules of the game) plays a great role in the defining the options that the different sizes of companies have at the time of trade openness processes.

Then, from this view it is possible to imagine contexts in which large incumbent companies, operating close to the technological frontier, nevertheless operate within institutional frameworks characterized by high concentration and low competition, can contribute to the overall performance of the economy in a more efficient and effective way than what would happen in a context of greater competition and less concentration.

This is an important issue to be analysed in the Chilean case, given that in this country there are very few markets in which all of the firms are of the same size; size differences between firms has been cited as a central area of our research, given the empirical relationships between market power, elasticity of demand, and type of predominant collusion in the markets. As we showed above, the set of institutional relations between the sizes of companies is a central area to be analysed.

Another important element to be established in the Chilean case, is whether the virtuous relationship, commonly assumed as undeniable, between competition and innovation is effectively valid. If that virtuous relation is present, it would be correct to assume that the lower level of competition existing in the markets will tend to damage the innovation capacities prevailing in the economy, and therefore limiting growth. If that is not effective, we could assume on the contrary, which in those cases where a positive relationship between low levels of competition and high growth prevail. In that context, it could well be that the low levels of competition that have been consolidated since the opening could be promoting the good performance of the Chilean economy.

To analyse this point we will start, step by step, from the traditional analysis.

In first place, we will obtain a quantitative estimate of the elasticity of demand, a crucial step to solve the problem that we have raised previously.[169]
Its estimate is possible from the previous computed HHI but requires that we recalculate the Herfindhal-Hirschman indexes (HHI) in the following way:

$$(8)\quad \sum_{i=1}^{n} S_i^2 = \sum(1/n^*)^2 = n^*(1/n^*)^2 = (1/n^*) = HHI$$

Where S_i is the market share of Firm I and n^* the equivalent number of equal-sized firms that yield the same value of the HHI calculated above, this means that n^* is simply the reciprocal of the HHI.

$$n^* = (HHI)^{-1}$$

Now, it is possible to use this n^* to obtain Ɛ, where:

$$Ɛ = n^*Ɛ$$

Using then the estimates of the HHI which utilise Chilean IRS sale´s data, the estimated demand for the whole of a market composed of five segments of companies (micro, small, medium, big and mega) in the Chilean case, 1990-2009, would be on average:

$$Ɛ = -(2.47)$$

Values of price elasticity which evolved between 1990 and 2009 were (-2.67) and (-2.02); with a maximum point-value of (-2.72) in 1994 and a minimum point-value of (-1.88) in 2008.

169 Data and calculation´s method are reported in appendix III

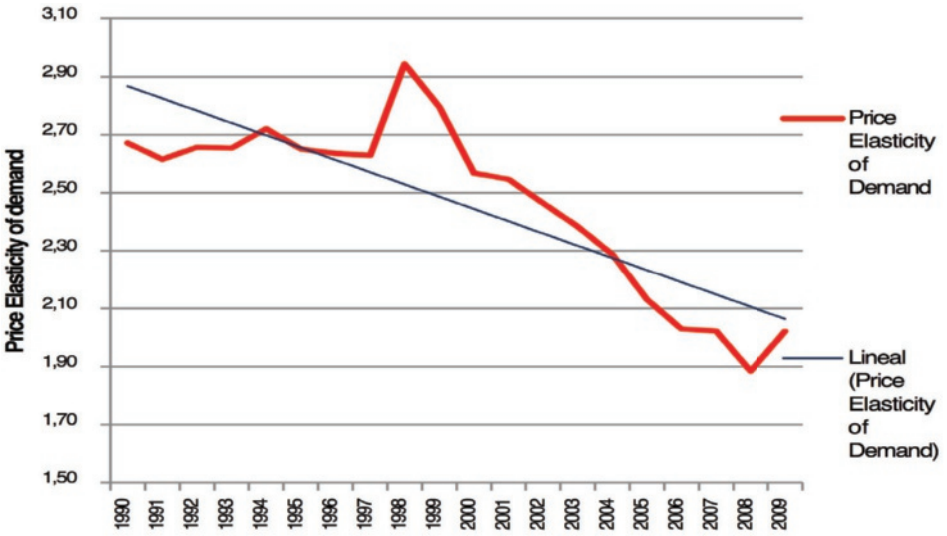

Figure 5.5. Price Elasticity of Aggregate Demand
Source: Author´s elaboration based on INE and IRS database, 1990-2009.

As Figure 5.5 shows, the price elasticity of demand facing the Chilean markets, has been decreasing over time as parallel to growing market power of larger companies. If such information were estimated by sector, there would be some differences in level between production branches. However, given the concentration of sales (85%) in little more than 1% of the companies, it seemed far more relevant to focus our analysis on the concentration in the segment of large companies. If LSE sold 85% of total sales, this ultimately explains the price elasticity of Chilean economy sector by sector and also in an aggregate level.

The declining price elasticity of markets and the high levels of economic concentration existing in the Chilean economy are a phenomenon that has been deployed simultaneously to trade openness. However, the presence of some causal relationship between these phenomena, as well as their consequences at the level of productive chains and market governance has not yet been fully analysed by us.

In order to establish in a more accurate way what the nature of the relationship between concentration and market power, a modified version of the Lerner index is frequently used (Aghion, Bloom et al, 2005), named L_2, in which:

$$\textbf{(9)} \qquad L_2 = S / (\mathcal{E}_m + (1-S) * f)$$

The parameters that make up L_2 are: the price (P), the marginal cost (MC), the market share (Is), the market price elasticity of demand (ε_m) and the supply elasticity of the competitive fringe (f).

These parameters measure the countervailing power of consumers, their willingness to do without the product or service if the price increases, as different from the firm's price elasticity of demand (ε) which measures consumer willingness to substitute products from other suppliers when a firm increases the price. Finally, yet importantly, (f) measures the change in the amount supplied by existing or new competitors due to a change in the dominant firm's price.

L_2 is a powerful index whose higher values indicate the presence of a great amount of market power; however, L_2 index value can rise for at least three different reasons:

1. Market share increases,
2. Market price elasticity of demand falls, and/or
3. Competitor supply elasticity falls.

We have already provided in the chapter information that shows that market share of large companies is growing, that price elasticity of market demand is declining and that the market share of small enterprises (weighted by their ability to offer competitive products when large companies are increasing their prices) has been declining. Thus, it is possible to conclude that, in the Chilean economy, the L_2 values are rising and therefore the concentration has resulted in greater market power for large companies.

The only way to assume that the Lerner index is decreasing and hence the concentration decrease along it would be which, supply elasticity of the competitive fringe is situated in such magnitude that compensates **S** and ε_m variations. However, we know that not tradable products (the most important component of general PCI) are composed basically of services operating in markets in which practically there is no serious competition, therefore the hypothesis which assume high demand elasticity and an increasing market share of the MSME (and hence of Lerner index) is highly unrealistic.

Growing market power of LSE, has been generating important mark-up increases, especially in the area of non-tradable products which, given the presence of abundant practices and institutional arrangements that are not conducive to their operation on a competitive basis, face the more inelastic segments of demand (Campos et. al, 2006; Alvarado y Spolmann 2009; Serra, 2011; Bitrán, 2011; Solimano, 2012; Goyenechea, 2016).

Given these dynamics, non-tradable domestic goods´ prices are growing beyond the increases in the international prices of similar products and very across the evolution of Domestic CPI and the International CPI.

This means that the economy as a whole is moving away from a competitive pattern and that the levels of competition existing between companies operating within the country, far from expanding, is actually reducing. Conversely, the market power of the raising market power on productive chains and economic sectors has promoted emergence of institutional arrangements who regulate inter firm size relationship under terms defined only by the mega corporations whose market power has been increasing, vis a vis trade openness.[170]

That situation must be explained by the fact that in Chile the antitrust regulations and the institutions that should exert the power of law enforcement, able to regulate the interactions between companies and between firms and consumers, were only nominally present during the dictatorship period (Ramirez, 2015). During the analysed period (1990-2009), they have started to be rebuilt, but redesigned antitrust institutionally has shown a great laxity, especially if it is compared to the antitrust laws in operation in the USA, or the E.U. (González, 2009; Bauer 2011).[171]

This weakness has permitted installation of several institutional arrangements imposed by large scale enterprises, which have frequently weakened the competitive status of non-incumbent small firms, without benefiting customers of large companies. The final result of the lack of a real antitrust regulation (supported in the neoliberal idea

170 Within an export-led growth on such a scale as exhibited by the Chilean economy, the least of all evils' scenario would be that, after trade openness, the relative participation of each size of company that existed before openness would stay constant. In the best case, we should have observed that this increment should enlarge the market share of the smaller Chilean companies, which are, after all, 98.5% of the total firms, regardless of increases in the absolute value of sales in each stratum.

171 Bauer (Op. cit.: 26) analysing the strengths and weaknesses of the Chilean Antitrust Law and the role played in its development by the neoliberal economists of the Chicago School states that*: "The American economists took the seeds of American antitrust policy and transplanted them into the Chilean context so that their application and development would be meaningful and effective. Such an approach recognizes the similarity of the broad aims of competition laws – to ensure competitive markets – while simultaneously accounting for local objectives. By pairing with a local university* (The Pontifical Catholic University of Chile.)*, the Chicago School economists also invested local academics in the success of the competition law, incentivizing their cooperation in the creation of a competitive market economy in Chile*". But even assuming the best of intentions in all that effort, Chilean antitrust law is so far from resembling to the effectiveness of the USA legislation and even less to the EU one.

of "market deregulation"), has been the expansion of market power of LSE and the generation and capture by them of high and rising economic rents.

Indeed, despite the fact that, in the Chilean case, the economic concentration and the fall in the elasticity of aggregate demand are simultaneous phenomena, this evidence is still not enough to conclude that the concentration of the economy and the oligopolistic behaviour of the prices system, have caused a bad performance of the Chilean economy as a whole. However, even though from 1997 onwards the growth rates have been increasing downwards and the economic concentration increasing, this in itself is not a clear indicator of "poor performance"; even if said term is understood as a suboptimal growth of the Chilean economy, in relation to its potential growth, expected as a result of the trade openness and liberalization.

To portray the real situation of the Chilean economic performance, it is necessary to deepen our analysis in order to expand the range of conclusions that can be drawn from the evidence collected.

5.8. The Asymmetric Evolution of the Firms´ Market Share

Twenty years after the end of the dictatorship, the economic results of Chile, at least during the golden period ending at 1997, have been noteworthy in terms of output growth, however have not been outstanding in terms of the distribution of this growth, not in terms of the origin of production, nor the destination of this. Specifically, in terms of the origin of the GDP, it is observed that this is has been concentrated in a small number of companies. In absence of statistics that allow a direct look at the origin of the GDP according to size of companies, the evolution of the market share of each firm size will be used as a good proxy to identify the product´s origin of each segment's size.

In the year 1990, the 5,160 LSE operating in Chile this year (1.2% of total) accounted for 73% of sales; however, in 2009, 84.2% of sales were concentrated in 1.5% of operating companies (10,174 Larger Enterprises). Conversely, while in 1990 MSME segment which included 421,181 firms in 1990 and 787,844 firms in 2009, (98.5% of the total number of firms), generate this year 27% of sales, however the year 2009, these smaller firms generate only 16% of sales.

The asymmetries are evident, but they reflect not only economic concentration but also the severe difficulties that exist to reverse this situation.

If the MSMEs increased their sales by 1%, this would be equivalent to a rise in market share from 15.8 % to 16%. For large companies, this would mean a climb from 84.2 to 85.2%, which is almost five times greater. In fact, larger enterprises are required to widen their market share by 1%, a rise in sales of 21 US million dollars, but the smaller ones require sales of only 8 million US Dollars.

That means that each large enterprise requires a growth in sales of 781,000 US dollars, but the small enterprises require a rise of only 10 US dollars each. This situation presents us a double dilemma. From one side, shows us that the major expansion of market share of the LSE (11% over 20 years) is associated with absolute values of sales much larger than what the percentage changes may suggest and across suggest caution on the utilization of indicators that generally are used to measurement of economic concentration.

In the area of use of concentration indicators, as Hymer and Pashigian (1970) assess, in those contexts in which exist hugs levels of concentration, *"will be more difficult for a dominant firm to increase its market share by one percentage point than for the fringe firm. If the large firm actually does increase its market share by one per cent, it should therefore be weighted more than a one percentage point increase by a small firm".*

Thus, given stratification by size of the group of companies, it will be necessary to take into account associated bias with the lesser difficulties of the MSME to increase its market share and the increased difficulty faced by larger companies.

Simultaneously, it should also take into account that when, despite the above, dominant firms manage to increase its market share by 11%, impact on the concentration will be even bigger than it seems on a first glance.
The five groups in which data was disaggregated in this research were, on one side, micro, small and middle-sized enterprises, and on the other side LSE Firms (a segment that includes in total 5,160 firms in 1990 and 10,249 firms in 2009).[172]

172 In 1990, Chilean enterprises numbered 426,341, whilst in 2009 this number had risen to 798,073. Estimates were made for each one of the five groups and for the sixth segment that we denominate "Large Enterprises (2)". This segment is formed by the sum of the large companies and the mega corporations. However, within it, the most relevant segment is the "mega enterprises", because in spite of their small

Within this last group, we must distinguish two sub-groups, the "Big Enterprises" (BE) and the "Mega-corporations" (MC).[173] MC are a small cluster of 2,715 firms that in 1990 accounted for 54.6% of total sales in the Chilean economy and in 2009 were composed by only 1,536 firms, but which, at that time, accounted for 67.6 % of total sales of Chilean economy.

Lastly, within LSE we must also differentiate the BE cluster, another sub-segment that in 1990 accounted for 26% of total sales and in 2009 only 17%.

number (i.e. slightly more than 1,536 firms in 2009) they directly carried out almost 68% of the total sales of the economy. Unfortunately, the bulk of large corporations (and the MSME) are not listed on the stock exchange. Therefore, information does not exist which would enable us to properly establish the presence of dependency relationships between MSME or Big Companies and Mega companies. There is however, casuistic information enabling us to conjecture that, in the case of more profitable segments, this dependence is quite high (DIPRES 2015). That situation would indicate the presence of a higher level of concentration than the ranks obtained using the IRS statistics.

173 In our opinion, when analysing the Chilean economic concentration, it is much more important to focus on the size distribution than on the sectorial one; for this reason, we utilised the segmentation in this research. The boundary that separates the different kinds of enterprises will be sales level (used as a proxy of size), criteria widely used by the Chilean authorities. The official level of sales that separate micro-enterprises from small enterprises are 25,000 UFs, the limit of small enterprises with medium-sized companies are 50,000 UFs, the separation between these firms and large companies is given by the 100,000 UFs of sales, while mega-corporations are those that annually sold over 1,000,000 UFs. The UF is a currency unit of constant value that, at December 31 of 2009, amounted to US $40.

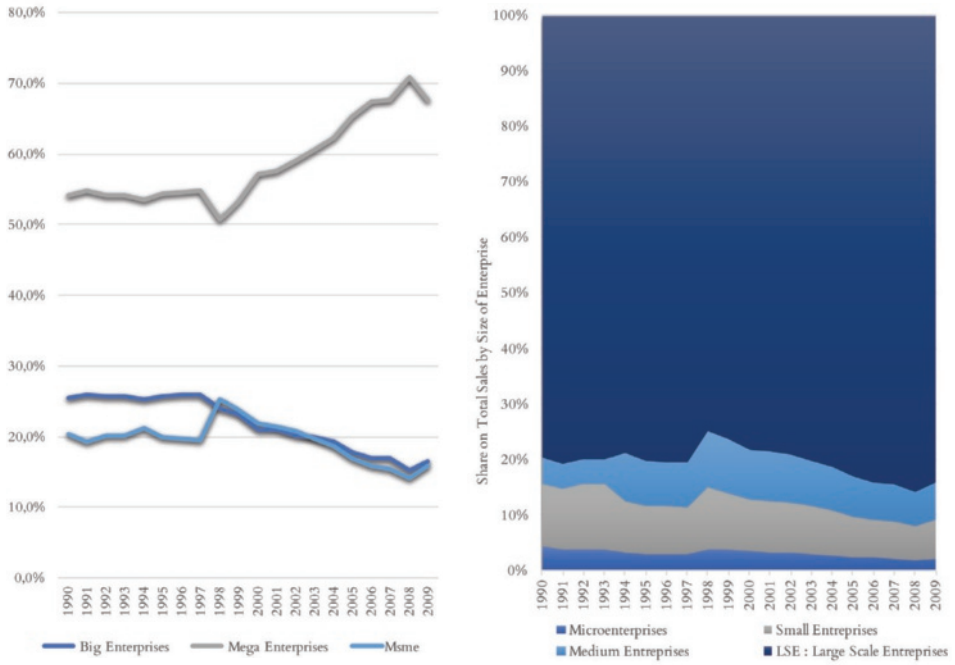

Figure 5.6. Market Share Evolution by Size of Enterprise
Source: Author´s -estimation using database of Chilean IRS, 1990-2009.

Figure 5.6 depicts the market share behaviour of the different groups of companies throughout the period under analysis. Immediately, it is clear that the only segment that actually improves its market share is the Mega corporation group. On the contrary, both MSME and Big Enterprises have been losing participation in a sustained way. From Figure 5.6. may be visualised that the Big Firms, after initially starting with a market share 25% higher than the MSME share, have declined consistently since the end of the 1990s, maintaining a market share regressive tendency virtually identical to the MSME share evolutionary trend. Despite they are in the group of largest companies in the country (without possess ownership relationships with major business groups, they share the fate of MSME.

Looking that Figure, we can confirm the strong sales concentration in the LSE. When the sales performance of the MSME are compared in relation to the performance of BE and MC that tendency is clear. When sales of LSE are split among Big and Mega enterprises, is possible appreciate that BE (after the breaking point of Asian crisis) present the same declining market share than MSME.

Then, it is clear that the flourishing sales evolution of Mega Corporations, is the area in which is reflecting the asymmetrical market power prevailing in Chile between different scale of firms. Once those general evolutionary trends are clarified, it will be useful (the precautions of the case) to estimate an HHI concentration index that will let us quantify these tendencies. In order to do that, we use the aforementioned Chilean IRS database from where may be estimated the annual variation of market share of all Chilean companies.

The HHI ranges from zero to one. The U.S. Department of Justice considers a market with a result of less than 0.1 to be a competitive marketplace; a result of 0.1–0.18 to be a moderately concentrated marketplace; and a result greater of 0.18 to be a highly-concentrated marketplace. Estimation of HHI is a method of summarising the degree to which an industry is oligopolistic and the market share controlled by the largest firms in the industry.

Some problems related to HHI stem from the fact that, for a given year, this index is only calculated by using that same year's data. Therefore, HHI is not an adequate tool to predict the market concentration likely to occur in the future. This is largely due to the fact that the market shares used in calculating HHI are unpredictable, but in our research, we are interested in evaluate a given period (1990–2009) in which the relevant issues involve the estimation of HHI produced throughout the period, being less relevant to any kind of forecasts.

If HHI shows a higher degree of concentration, it would mean that concentration was positively correlated to trade openness process, and not negatively as neoclassical-neoliberal views sustain. Market shares are highly influenced by the size distribution of an industry.

When enough data is available, it can potentially provide a good simulation of the size distribution of markets made up by a big number of firms. In our case, we had access to information corresponding to universe of all Chilean companies, with a level of disaggregation of five digits and separated by size. That database gave us information that allowed us to quantify the annual firm's sales volume for each year and therefore let us make an estimate of the market share of each sector or size of company, with a high level of disaggregation.

Our calculation of the HHI was performed primarily with five sizes of companies: micro, small, medium, big and mega, measuring the level of concentration or dispersion of sales among these five kinds of firm sizes.[174]

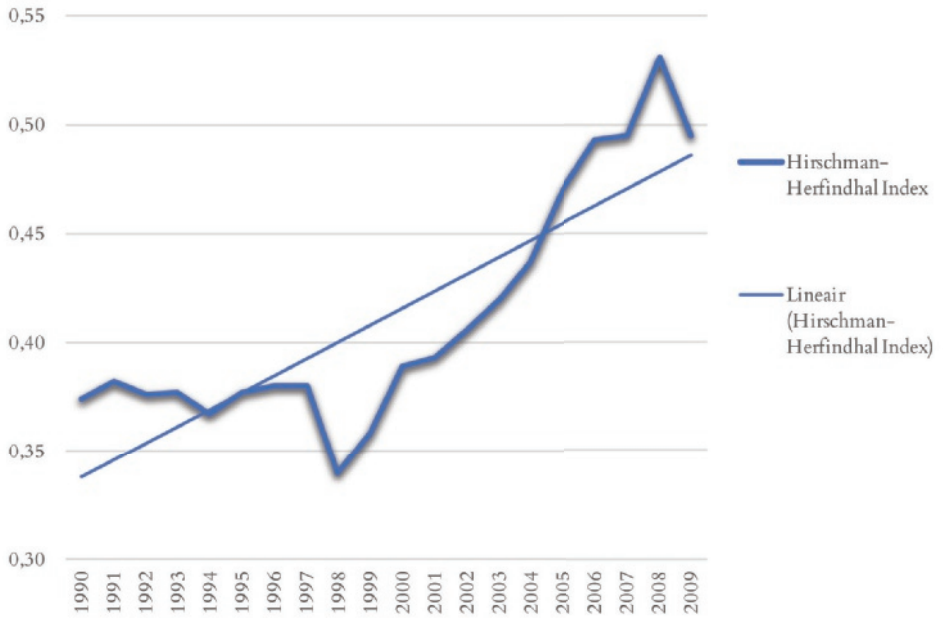

Figure 5.7. Evolution of HHI Concentration index
Source: Author´s elaboration based on IRS data, 1990-2009.

As we have already stated, in general markets are considered to have a high concentration when HHI is over 0.18; moreover, in the United States, a concentration level involves antitrust actions only when the HHI exceeds 0.25.

On the other hand, the European Union prefers to focus on the level of change of HHI and not its absolute value.[175] Nevertheless, in both cases, levels over 0.3 are

174 The identification of size is guided by the criteria used in this regard by the Chilean Government; given the existence of a relevant market concentration, the indices calculated by us allowed us to measure the specific magnitude by which the Chilean markets are controlled by large corporations with elevated market power.

175 Chilean antitrust actions do not refer to concentrations by size of companies, but only to sectorial ones. However, when in a country like Chile in which larger companies which, constitute 2% of all firms concentrate nearly 85% of sales domestic it is not sound to argue that that is an issue outside the

considered extremely high, reflecting the presence of an unacceptable level of economic concentration; levels close to 0.4 are out of consideration in USA and EU, does not permit the possibility of some enterprises showing HHI of 0.49%, or in the weighted index, of 0.46%.

The absolute value of HHI, as Figure 5.7 show levels of concentration extremely high. However, giving a greater weight to the presence of competitive markets involving the 98.5% of enterprises (MSME) can be misleading when the 1.5% of remaining business concentrates 85% of sales of the economy and that ratio continues growing in a systematic way.

All that information show that in the Chilean economy there is a clear phenomenon of high concentration and presence of oligopolistic markets. Thus, our analysis of the relationship between trade openness and market competitiveness lets us conclude that opening is not associated with a process of market competition improvement. In some ways, this conclusion was initially suggested by our analysis of the internal price performance of non-tradable products, and can now be established on the base of the high level of concentration and market power of mega corporations that HHI demonstrates.

The lack of a competition environment, seriously limit any intent of chain upgrading, eroding the grounds of adequate institutional governance. On the contrary, within the chains it establishes a fertile field to destroy linkages between different sizes of firms, fostering vertical integration among firms of the same size and related ownership.

5.9. Is the unrestricted promotion of market´s competition a residual bad practice that should be revisited?

We have analysed in the previous chapter of this thesis, how in Chile, during the analysed period, there has been significant growth in the market share of large enterprises. We have also shown that this expansion has produced a sharp process of economic concentration and we have assumed that is highly possible that this process be, to a great extent, related to the fact that large firms are operating in the more

scope of the antitrust authority, given that this issue that does not can considered as related to sectoral concentration. Nevertheless, the HHI estimations that use sectorial data, find even greater sectorial concentrations than those than we have estimated using the variable "size" (e.g. Solimano, 2012:127-129).

inelastic segments of the demand curve. Nevertheless, even if is clear that those large firms would be expanding their mark-ups and market share, this situation does not itself explain why they have achieved such levels of market power in this small and open economy.

The questions that try to answer this question are basically two, each pointing to different hypothetical inquiries.

1. It is the deployment of strategies operating off-market- reducing levels of competition by LSE in order to increase their market power- generating rents and thus putting a brake on the growth path of the economy?

Or, on the contrary,

Is it that the strong economies of scale and the greater proximity of LSE to efficiency frontiers- the variables which have induced a strong GDP growth dynamic based on innovation- have permeated though the Chilean economy as a whole?[176]

When trying to answer these two questions, we can find at least three large groups of explanations, all of them associated to specific forms of institutional arrangements associated to different kinds of transaction costs:

- A first line of analysis interprets the price gap, which is on the basis of concentration process, as a product of the presence of transaction costs preventing arbitrage (Engel and Rogers, 1996).
- A second line of analysis emphasises the importance of local non-traded retailing costs, or in other words, the influence of pricing mechanisms dominant at the retail level (Burstein, Eichenbaum and Rebelo 2005; Pinelopi, Goldberg and Verboven 2005).

176 These are questions of crucial importance, but they are not part of the core of polemics between neoliberal economists and their adversaries. In fact, when neoliberal economist's discuses about concentration, basically, they emphasise, as explanation of the LSE success, the role of economies of scale and the relative efficiency of these large companies. On the other hand, paradoxically, Neo-Schumpeterian economists tend to place themselves "on the right" of the neoliberals, delivering more structural and definitive justifications about concentration, visualizing large companies as the vanguard of development and modernization process, and viewing the phenomena of concentration as a less relevant issue, that does not modify their judgment about superiority of development strategies based on the disappearance of MSMEs and peasant economies and on the overwhelming hegemony of incumbent business economic.

- A third line of analysis distinguishes pre-innovation incomes from post-innovation incomes, assuming that innovation is an "escape route from competition" in which the effects of liberalization on entry, on innovation and productivity, ultimately depend on the distance between incumbent domestic companies and the global technological frontier (Aghion, Burgess, Redding and Zilibotty, 2003, or Aghion, Bkundell, Griffit, Howit and Prantl, 2003).

In relation to this point, the first two groups estimate (focusing, each one, on the presence of different kinds of arrangements) that the growth of the market power of some companies is inexorably associated with a decline in output. On the other hand, the third interpretation estimates that there are causes (that are not always institutional in nature) that generate exactly the opposite effect, enabling economic concentration to translate into higher GDP growth rates.

Inside the first group, Engel and Rogers (op.cit.) stress the relevance of transaction costs that prevent arbitrage. But, if the trade openness is not reducing or eliminating these transaction costs, this means that the effect of international prices has not been able to re-define resource allocation processes in the way forecasted by neoliberal advocates of Chilean model. That situation is not easy to explain, at least within the neoclassical or neoliberal paradigm, which considers that the presence of transaction costs is not an element capable of counteracting the impact of the modification of the system of relative prices induced by trade openness.

The assessments of some already quoted authors (like Pinelopi et al.), emphasising the influence of increasing costs in non-tradable goods and their impact on the mechanisms of the retail pricing, are only reasonable in the context of a closed economy or one in the initial process of opening, but not in the context of the Chilean one, which has perhaps the longest trajectory of full trade and financial openness in the world.

Furthermore, although there is some evidence of the after-effect of retail mark- up on the PCI of Chilean economy, there is not enough evidence allowing us to conclude that the oligopoly forces of the Chilean economy are only concentrated at the retail sector and that they are the key variable influencing an eventual resource misallocation in the economy as a whole.

And, even while maintaining an open economy with a free and flexible price system, after 40 years of radical opening, Chile is not yet in condition to use prices as a signal

that drives the resource allocation processes. That situation implies that new relative prices induced by trade openness are facing an institutional context that is more influential than the relative price system, a situation that confronts the core of the neoliberal view and also some core neoclassical assumptions.

Along the same line, De Loecker and Eeckhout (2017) use similar arguments applied to the case of the USA. They report that price fixing above marginal cost by listed companies in the United States has been increasing since 1960, and particularly after 1980. They also report a significant increase in pricing practices on the part of large incumbent companies, endowed with great market power, which currently dominate sales, profits and production and whose use of labour is low, compared to other companies and industries. As these oligopoly companies do not have to confront competition, these do not invest at desirable levels and, therefore, productivity decreases or cease to exist.

These authors point out that, between 1950 and 1980, at a global level, price fixing was more or less stable at around 20 percent above the 'marginal cost'. Since 1980, however, price fixing would have increased significantly. On average, in 1980 companies charged only 18% on marginal cost, compared to 67% in 2014. This important increase in profits, they argue, is consistent with an increase in market power of large corporations. "In perfect competition, total costs and sales are identical, because there is no difference between the price and the marginal cost. The degree to which these two numbers – the relationship between sales and wages and between total costs and wages – begin to distance themselves is an immediate indicative of market power" (op. cit.).

However, from the point of view of other authors (Aghion et. Al.; 2003), the technology and market conditions (or their interaction) would have evolved to increasingly concentrate sales in companies with products of superior quality or higher productivity. Allowing the most successful companies to control a larger market share. Then, these incumbent companies would be more profitable, but they would have a lower relative share of wages in total sales or in value added.

As a result, the aggregate share of labour decreases as long as the weight of the "super-star" companies grows in the economy. According to this view, the concentration of sales (and employment) would have increased from 1982 to 2012, but the industries with the highest concentration are those where the most pronounced falls in labour participation have occurred. From that perspective, the perceived decline in labour participation in GDP is a normal phenomenon linked to globalization.

They assume that worker's remunerations in developed countries would lose ground to GDP due to the migration of large companies to countries in which the labour cost are lower, and additionally due to automation and robotisation. Given that, they assume that the fall in labour participation, is mainly due to a reallocation of labour towards falling off companies which have lower intensities of labour use, instead obey the reduction of labour participation within the products sold by most companies.

However, contrary to their view, it would not be unsound to assume that the reciprocal increase observable in the share of capital in the GDP, would not be due to globalization or automation, but rather to the setting of high prices by companies that, contrary to what happens in the context of normal competition, are obtaining additional benefits beyond their "costs".

The presence of arrangements that enable firms to operate in inelastic segments of demand curve appears as a central element of this last kind of hypothesis. Nevertheless, within that views, those elements that emphasise the oligopoly market organization, play only a minor role, given that within their paradigm the view that the forms of organization of markets corresponds to a process of intentional building of institutions, is a process constituted by actions of a political rather than economic nature and that are developed from an arena very distant to the markets, and perhaps for that reason, do not manage to adjust with their perspective of analysis any of these problems.

Our analysis is faced here with two rather clear options, those who argue that the concentration processes are a normal phenomenon associated with the globalization and technologizing of the economy, and, on the other hand, those who believe that this phenomenon corresponds to the consolidation process of institutions of oligarchical nature. The latter would favour a concentration of economic and political power in the hands of large business groups, whose dynamics of capital accumulation impede the deployment of virtuous growth processes based on innovation and productivity, and not only on extractive dynamics.

It is not necessary, in our opinion, to use sophisticated econometric tools to elucidate the controversy about the virtuousness or viciousness of concentration in the Chilean case.

The approaches that provide a more favourable view of the concentration processes, assume that the impact of competition and free entry to markets varies with the dispersion of technology in use within each industry. In simple words, the problem

would be the distance to which each industry is located in relation to the technological frontier. These approaches to the subject, estimate that an exaggerated emphasis has been placed on the impact of competition on post-innovation incomes, underestimating the role of pre-innovation rents. Thus, by differentiating different behaviours based on that, they come to the conclusion that there is an inverted U-type relationship between competition and innovation. It makes it possible to assess in different ways the competitive requirements of each market, depending on the point that the economy is placed in said relationship.

If the competition is more intense, it can produce more innovation (that is, after all, a greater "escape competitiveness"), because it reduces pre-innovation rents by more than it reduces post-innovation rents (Aghion and Griffit, op cit: 3-5). The net effect of the process will depend on which of two effects dominate: "rent dissipation" or "escape competition". Which in turn will depend on the technological variables associated with the distance of each sector or company in relation to the global technological frontier.

The farther away from the border they are, the greater will be the damage inflicted by a commercial opening, since the incumbents (close to the border) will be able to survive and face the innovating challengers, in sectors such as the MSME or the peasant economy, placed so far, will have several difficulties to confront external entry.

Translating this hypothesis to the Chilean case[177], we should conclude that the large companies that dominate the markets do so by their greater proximity to the technological frontier, inversely the decline of the MSME would be explained in turn by its distance to the border.

As the effects of "income dissipation" are less than the effects of "scape competition", this should lead to the evaluation of concentration phenomena as positive, a fact which could be explained by a greater technological capacity of the incumbents defended by the innovation processes. To oppose it would be tantamount to defending the backwardness against progress, the "economic populism" and against "non-impartial and technical use of economic theory."

177 To be accurate, Aghion and Griffith, sustain that his proposal it is valid only in advanced knowledge-based economies, where the growth potential of factor accumulation and limitation has been exhausted and frontier innovation becomes the main source of growth (op.cit:2), and in any moment, suggest a possible conclusion´s extrapolation to development economies like the Chilean one.

Taken to its extreme that hypothesis would imply forgetting the specific modalities by which the economic groups whose companies were formed, we are told to the contrary that this leadership has been produced by its greater proximity to the technological border, forgetting that all the official information emanated from the Chilean government, shows that technological innovation is almost non-existent in the country.

According to data from the last National Survey on Expenditure and Personnel in Research and Development, designed by the Innovation Division of the Ministry of Economy and the National Institute of Statistics (INE), R & D expenditure in the country would be equivalent to 0, 39% of the GDP, lower figure and very far from the 2.4% that the countries that make up the Organization for Economic Cooperation and Development (OECD) allocate on average.

So that, even the highest government authority on innovation, Eduardo Bitran, executive vice president of CORFO, told the press: "*In Chile our companies do little innovation. We are very far from the standards of the OCDE, there is even a declining trend… Technological innovation and innovation in R & D, is not in the business strategy of our companies*"[178]

In other words, there is no greater evidence of innovation that supports the dominance of the markets by the incumbent economic groups. Chile is the main producer of copper in the world, but its mining technology is provided by Canada and Australia. It is a large producer of pulp, but the technology of its industry is provided by New Zealand. The fishing sector in Chile is one of the largest industries, but its technology is late in terms of capture technology and at industrial processing level. Even more so, in the transformation of the fish caught for fishmeal, with the use of processing plants that would not comply with the minimum standards of Japan, the USA or the EU.

The most inefficient cases of innovation policies implemented by the Chilean government are focused on small and medium-sized high-tech companies, which could be defined as close to the global technological frontier, that is, the picture seems to be the exactly opposite to the one described above, in such a way that it is very difficult to find information that validates the Neo-Schumpeterian hypotheses.[179]

178 See: "La Tercera" newspaper/ 22/06/2015.

179 See: http://www.economia.gob.cl/wp-content/uploads/2016/08/Res-Ejecutivo-START-UP-

However, that approach has played a very important role in incorporating the neoliberal topics within the centre-left technocracy. In general, this approach clashes with a common sense built from the observation of the Chilean business world and the operation of its economy. A fact that, in addition to the lack of appropriate data to test the credibility of new hypotheses linked to the NEG theory, are interesting to teach in the academic world, but that generally represent few opportunities to be translated into practical public policies.

5.10. Trade Openness, Competition and Non-Market Activities

In general, in a competitive context, the price is given and the production and sales constitute decisions to be taken depending on the price. When a company wishes to circumvent this context, there are only two strategies (isolated or combined) to develop improvements of its competitive position:

- The first strategy is to use the internal resources of the company with greater efficiency and effectiveness in relation to its competition (Leibenstein, 1966).
- The second strategy is to try to differentiate product (and related services) or segment markets (Galeotti and Moraga-González, 2003) and boost it on that basis, develop an acceleration of its production and sales to surpass its competitors, thereby eroding their customers' and external suppliers' powers of negotiation.

However, these are only the two large generic options, representing a multiplicity of choices resulting from the combination of both alternatives and their respective sub-options. Nevertheless, in each country, not every form or combination of options is legal and permissible and their relative success depends largely on levels of competition in markets and on the rules of the game that strengthen them.

If a company is embedded in a highly competitive context, in the long run, either of these two strategies is viable by itself. In competitive contexts product differentiation-market segmentation and excellence in production and management can be quickly imitated and require great effort and large capacities within the companies to keep them as a permanent and successful action.

In spite of those options, a shortcut might be to obtain support from the State in exerting influence in the making of laws, in order to consolidate a certain market position. Therefore, in order to circumvent the market competition, the path of bribery, underground lobbying, and traffic of legislative and administrative influences, rather than innovation and the development of competitiveness, has become the favourite method of large Chilean incumbent companies (Garin, R; 2016).

If a company innovates by opening new markets, producing different services or simply achieving a greater cost-efficiency, that means which is achieving a high but legitimate level of market control, obtaining a temporarily advantageous position. Nevertheless, after a short period of time, the force of competition will cause a return to the original competitive situation, insofar as innovation and efficiency can be absorbed by the market and made available to all players.

However, if regulation is lax about what is legally permissible in terms of non-competitive practices, we will see that, soon enough, which that firms using business models based on mix: innovation-differentiation-segmentation-efficiency, will not obtain real competitive advantages over the companies with high market power. On the contrary, non-market economic intervention of incumbent's firms on the design of rules and regulations will tend to be the variable that should enable the continuous growth of overbearing enterprise´s participation in the markets beyond of its competitiveness, because this process enables them to consolidate a monopolistic or oligopolistic position by means of those non-market arrangements.

Thus, by following the pathway linked to lobbying and regulatory capture influence, it has been seen that many corporations have consolidated the generation of stable economies of scale that create competitive advantages which constitute an automatic and insurmountable barrier to their competitors.

That happens because the main goal of those economic actors is to produce strong and sudden increases in the scale of operation. Mergers and acquisitions are the essential mechanisms that allow these leaps of scale. It is the presence or absence of the regulatory mechanisms of these processes, which will determine the success or failure of some forms of the "escape competition effect" usually attempted by incumbent corporations trying to obtain some market power.

In this option, mergers, or the acquisition of competitors, end up being the mechanisms that enable the realisation of these strategies. If a company based its development on innovation and the efficient use of its internal resources but there is a strong constraint to their non-market activities, this firm will probably remain on its route permanently.[180] In this case, the economy would soon be rewarded by presence of highly competitive markets, with all the positive consequences in terms of allocation of resources that this would entail. However, to promote such an option would require the legal closure of those arrangements that try to develop competitive advantage by eroding competition within the markets.

5.11. Tree key dimensions of Chilean business fabric in which predominate an exclusion dynamic that limit productivity

The points outlined above aim to show that mere trade openness is so far from possessing the necessary strength to build a new system of allocation of resources in the economy. The disappearance or reduction of trade barriers does not lead automatically to ensuring that companies acquire better access to markets, especially in those cases in which a small number of incumbent companies govern those markets.

5.12. Market access

Without the existence of equal opportunity available to all firms, to integrate themselves into productive trade networks and into institutionally consolidated business alliances, it seems difficult to expect that the weakest companies can achieve the coordination and business strength needed to improve their participation in the generation and distribution of added value (Ruben 2006: 13-14).

180 Firms operating in a competitive market have incentives to innovate to "escape from competition" and enjoy higher market shares (that modality of "escape-competition effect" can be read about in detail in Aghion et. al. (2005)). In general, firms within a competition framework who wish to enjoy monopoly rents, innovate to protect their market position and discourage entry by potential competitors. Several researchers have focused on the interaction of these two opposing forces: innovation and competition. As a result, even today, it is not clear whether market competition increases or discourages investments in R&D (Petropoulos, 2015). However, we are referring to a wider situation that includes strategies that originated in non-competitive contexts, in which the firm's strategies to "escape from competition" included market and non-market activities tending to avoid the introduction of higher levels of market competition.

Within that context, it is not sound to expect that companies may improve their capacity for production of added value. Either by the generation of products, processes or coordination improvements within the production and distribution chains (Gereffi and Kaplinsky, 2001; Gereffi et.al, 2002; Ruben et.al, op.cit: 15-16). However, in general terms, once the presence of severe distortions in the price system are established (especially in those sectors those that are more immune to effects of commercial opening), it would be normal to assume that demand price elasticity will tend to be very low (and decreasing).

At least that must happen in the main sectors of the Chilean economy but, as a result of the market power of some large corporations, is concentrated in the non-tradable sector and also dominate exports of tradable goods. There are no empirical bases on which to rely upon to demonstrate that the Chilean economy shows that kind of performance. On the contrary, over the years the demand has tended to become more inelastic, the economic concentration has increased significantly, and the market power of business groups has begun to become incontestable.

It is not the same as assuming that the neoliberal hypothesis as a whole has indeed been falsified. To do so it is necessary, first, to probe that evidence contradicts neoliberal hypothesis as a whole, and after that explore if others factors (e.g. institutional arrangements) are explaining price evolution rather than trade openness.

If we try to establish whether trade openness effectively reduces competition in domestic markets, the first step must be to establish the evolution of market competition levels over time. Then, we will try to establish if that degree of competition is associated with the presence of some kind of market power exerting limits on the deployment of market competition. Afterwards, our analysis will start by measuring levels of market concentration as a proxy of levels of the intensity of competition. Given that we probe the presence of highly concentrated markets and additionally, that minor levels of competition will exist within them.

Additionally, we have showed that the possibilities of achieving a better participation in the generation and distribution of added value, or a greater participation in the institutional arrangements that make up the governance of the markets, is not an option that is open to most companies, but only for a small group of these that control different markets.

Access and sustain in markets in which concentration levels exceed 50% (at least) is an impossible task for any company and it is not necessary to argue too much to agree that this is not due to technological or competitive superiority, but that the simple fact that the productive chains are controlled by a small number of companies, as shown by the disaggregation of the IOM developed in Chapter VII.

5.13. Chain Upgrading and Competition in Domestic Markets

In an economy with high levels of competition, each single company should have a similar share of the total sales. However, perfect competition is a theoretical hypothesis whose presence must be tested rather than to be assumed as an empirical fact (Facchini, Namini et al.; 2012). For this reason, we have focused (chapter VII) on the description and analysis of specific forms of market organisation that actually characterise the Chilean economy and only after that, we have compare the results obtained with those that, according to the neoliberal discourse, should have been achieved after the trade openness and liberalization.

Increasing operating costs, higher costs and personnel recruitment, and qualified labour retention are the main obstacles to the growth of MSMEs within the productive chains. The reality of the Chilean markets is highly unfavourable for them in each of these aspects.

The lack of competition and the tight control of markets by a small number of companies has produced in Chile institutions of economic governance that conspire against the upgrading of capacities for companies that do not belong to these dominant groups, which therefore look Constrained in their capacity for improvement, which, if effective, should be expressed through the expansion of their market share.

The quantitative information reported in this chapter shows that in virtually no sector is there an improvement in the market share of MSMEs. The lack of access to credit, or the high rates at which they must access it, translate into high operating costs that transfer surpluses to banks, limiting their growth, and even jeopardize their subsistence. The organization of the labour markets and the determination of salary levels from the LSE, prevents the MSME to provide workers of the best possible level, which are attracted by large companies, even though the remunerations paid to these do not exceed by much those of the MSME. If the set of institutional arrangements that have

placed the substantial state resources for training workers almost entirely in the hands of large companies, the exclusion table in this area is complete.

Finally, the predominance of a predatory business model in which, the linkages of the LSE with the MSME tend to be replaced by the vertical integration of related companies.] In this way, the MSME operates as an almost unlimited supply of suppliers to the LSEs, which extract their resources and inexorably reduce their market shares.

In this way, a circle is closed in which productive upgrading has been concentrated in the hands of a small number of companies. However, not being too prominent, they do not alter the extent in which the LSEs control of the markets.

5.14. Productive Chains Governance and Resources Allocation.

In Chile, the academic world is dominated by a neoliberal double discourse. On the one hand, free market is presented as a core value of the model, as it was the corner stone of their entire economic proposal. On the other hand, are deployed arguments that contradict this idea,[181] Neoliberals argue that, given the characteristics of the worldwide processes of trade liberalisation and the globalisation of the economies, the number of firms in a market or the sales 'concentration in a small group of them, are no longer enough to define a monopoly. Additionally, they asses that higher average profits concentrated in some sectors, is not necessary reflecting presence of economic rents, because they generally may be explained by the higher average size of firms who integrate these sectors.

181 In the USA economic mainstream, two schools of thought lead the market´s organization theory. One is the "structure-conduct-performance school" who asses that market structure determines the behaviour of the firms in the market, and the behaviour of firms determines the various aspect of market performance. An implication of this argument is that government should implement a relatively high-level competition policy, intended to limit strategic behaviour. The second one is the Neoliberal Chicago School; -the argument of this school is that anything one firm can do can be done by any other equally efficient firm, unless some higher power intervenes. In this view, the main source of monopoly power is government interference in the market place. Government, by intent or ineptitude, can prevent some firms from completing, to the advantage of other firms. Beyond the prohibition of naked collusion, there is little that government should do to try to improve market performance, on the contrary a laissez faire policy is recommended.

In Chile consequences of that approach were clear. Neoliberals declared that, given there are not enough Chilean big-size economic players, the country needs to produce strong economies of scale in order to compete with large transnational companies who are trying to control the regional markets.

They also assert that the rising market share of Chilean LSE is a defensive tool and cannot be associated, per se, with the implementation of monopolistic or oligopolistic practices based on market entry barriers or price´s discrimination. Within this perspective, neoliberals also argue that the old neoclassical way used to define "full competition" must be changed. Competition not necessary would be, in all cases, a desirable phenomenon; moreover, they think that "competition" and "monopoly" are concepts that should be re-defined (Paredes; 1991:21-46).

A major neoliberal point of view is that the real anti-trust issue is not related to how big is a firm currently, is but rather be extend to which there is a possible entry for a competitor. In this debate, in our opinion, neoliberals evade to define how effective, in their view, competition must become a market force generating adequate allocation of resources in the economy. In general, they assume that the presence of potential competition (based on the possibility of entry into the markets for new competitors) constitute a force potentially able to build markets acting as good mechanism of allocation. On that base, they deploy a tautological assessment: In a full open economy, external competition introduces, in several ways, potential competition in all goods and sectors; then, if there are trade openness, cannot survive significant monopoly or oligopolistic practices.

As we shall analyse next, the neoliberal answer lacks serious empirical grounds. In Chile, after trade openness there persist multiples business arrangements that, in other contexts, would be considered outside the law. Whilst the practices on which those arrangements are based, and which we define following Williamson (1996) as "governance institutions" continue to exist, this results in the exercise of greater bargaining power by large companies with respect to their customers and their suppliers. That governance institution would be at the root of the high concentration of Chilean markets (Cavalcanti and Facchini, 2005) but their characteristics are seen by neoliberals, not so much as a defect, but as a virtue (Ganuza and Pechlivanos; 2000). Institutions are a variable which is not considered relevant in the neoliberal analysis of Chilean case. For them the institutional environment is a given framework that once imposed by them, must act as a black box and not be scrutinized. Less importance

is given to institutional arrangements that complement the existing environment, supporting human capabilities and available technologies. Focusing only on prices effects, neoliberalism does not perceive that different institutions can have different effects and which, for that reason, institution may both promote as well damage the economic efficiency.

Institutions that are efficient in certain circumstances, in another context or in another time, may be highly inefficient. Moreover, institutions do not always adapt automatically in an efficient way to changes than intend to be reproduced, only as a result of their successes in others context, or given that they are promoted as best practices from a theoretical approach. Thenceforth, "bad institutions" (whether we refer to the institutional arrangements or to the institutional environment) may be highly dysfunctional to productivity and growth and to minimization of transaction costs.

Whether efficient institutions arise or not arise, will depend to a large extent on whether this is in the interests of those having the power to devise new institutions and, in the Chilean case, seem to be clear that subsistence of bad institution is not a result of a misleading theoretical approach, but rather to the presence of economic and social interests of some powerful actors.

The growth of the Chilean economy is evident at a glance. However, it is becoming clear that trade openness and market liberalisation, far from distributing new economic opportunities among different actors, concentrates them only in the most powerful ones. That is clear at the firm level. If small businesses were progressing technically and productively, this should translate into a higher market share and in benefits for them and for all society (innovation, productivity and growth). However, we have observed a trend in precisely the opposite direction.

Even considering the eventual presence of the lagged effects of innovation on productivity, if we compare Chile with developed countries, the available research shows low levels of research and development investment (R&D) in large scale Chilean firms (Benavente, 2004; ECLAC, 2007b). Additionally, the country's corporations have been very slow with regard to mastering new technologies (Alvarez et. al., 2010). This situation could help to explain why the Chilean economy has an extremely low

level of innovation and why any diversification of this economy is below what we would expect for a country of this level of GDP per capita.[182]

A context of high competition promotes innovation, diversification, productivity and growth, however, if the only purpose is growth and reaching of maximum levels of profits, the better way to progress is avoid competition and prioritize the State capture. This comprises several kinds of influence in the design and passing of laws, rules and decrees promoted from a large number of State institutions, including the executive, the ministers and the state agencies, the legislative and the judiciary, with the intention of benefitting specific private actors using illicit, illegal, and non-transparent forms of influence.

All outcomes of those activities must be implemented by means of institutional arrangements which include a specific set of tax exemptions, weak antitrust laws, concession of public goods, rule applicable to contract between enterprises, environmental authorisations, way to evaluate banking risks, and other competitive advantages made possible from the State. The use of these strategies obviously constrains any kind of innovation and productivity undertakings considered as being of "low profitability".

Once those specific institutional arrangements take legal form, they automatically ensure a shape- market relationships structured in an asymmetric way. The result of this situation is that, when large corporations use some combination of both strategies in order to gain dominant positions in markets, they no longer need to use technical progress as a driving force for their control of the markets. The transfer and diffusion of already acquired technical progress from them to the remainder of the economic fabric, constituted by smaller size companies, is even less necessary.

This state of affairs has enforced a heavy economic concentration and lack of diffusion of technical progress, factors which imply the introduction of powerful biases in the mechanisms of the allocation of resources.

Thus, it is sound to assume that in the Chilean case, as has been generally argued: in the literature (Mitton, 2008: 367-368), the concentration of economic activity in Chile has led to potential political distortions, individuals. Powerful families and business groups that control concentrated economic activities in the country have achieved

182 In 2009, Chile ranked 71 out of 124 countries that are part of the ranking of economic complexity index estimated by MIT. http://atlas.media.mit.edu/rankings/country/2009/.

to wield greater political power, thereby inducing policies favourable to their own interests which are not compatible with collective social interests.

Accordingly, the clearest expression of market powers obtained in this way is the reduction of competition by means of the expulsion of competing firms. In the Chilean case, this translates into the decrease in size of firms due to the reduction of their market share, the disappearance of a high number of firms and the increase of the business turnover, due to the reduction in number of new companies resulting from the expulsion of enterprises from the market each year.

This situation, highly dependent of the presence of neoliberal institutions of economic governance, as some studies reflect (Alvarez and Vergara, 2007), appears to be strongly present in the Chilean case. They find that in analyses of high sectorial disaggregation, evidence suggests the presence of an inverse relationship between mortality and size. These authors state that this situation implies the presence of the lack of some structural competitiveness capability of MSMEs, but that it is not a conclusion valid for all industrial sectors. The lack of competitiveness looks as though it may be related to sectorial insertion of MSMEs rather than to their size, given that this placing is associated with several institutional factors that exert influence on their market organisation and on their individual performance.

Perhaps one of the most important institutional arrangements is those that allow the firms´ access to credit in different condition, depending of their sizes and not of profitability of their projects. That is an essential factor that exerts a high impact on the survival probabilities of MSMEs.

Some studies (Román y Rojas, 1994) maintain that these kinds of negative impacts are associated with presence of rules of the game associated to neoliberal model, which consolidate imperfect capital markets, vis à vis trade openness and market liberalisation processes. It is possible that arrangements could become more relevant than the positive impact that both the new degree of exposure to international competition and the new relative prices would be exerted over the domestic market performance.

It is true that Chilean MSMEs have faced strong competition, mainly from Asian products because of the trade openness process. However, their decline is not only related to the low relative prices of Asian exports. Leading available research (Pagés,

2010), shows the influence in Chile of prevailing institutional arrangements over external competition, as the origin of MSME weakening.

Among quoted arrangements, are mentioned the lack of equal access to credit and markets, the non-existence of an adequate protection of free competition in domestic markets, the predominance of predatory economic models implemented by large enterprises, as well as the presence of multiple economic regulations that make MSME production costs significantly higher.[183]

This dynamic casts some doubt over the depth of structural transformation undergone by the Chilean economy as a result of the extended period of trade openness and market liberalisation process.

5.15. The Stagnation of Total Factor Productivity

The presence in Chile of institutional arrangement divorced to the collective's interests has produced serious allocation issues. The lack of diffusion of technological progress in the Chilean economy does not seem to be a problem linked to the profoundness of the trade openness process and either to the market liberalisation. On the contrary, it appears to be more related to institutional problems that distort the positive effects of trade openness and market liberalisation, independently of the profundity of these processes.[184]

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183 For instance, Chilean regulations for calculating the value of commercial licenses generate paradoxical situations. While a small neighbourhood shop of 6M^2 and monthly sales under USD 2000 must pay annually a license of USD500, a big supermarket of 40,000 M^2 and monthly sales exceeding of USD10 million, pays only USD15 annually (http://www.lanacion.cl/patentes-puesto-en-una-feria-paga-220-mil-anuales-y-supermercado-jumbo-679/noticias/2012-07-11/180058.html). Even more important than this is the differential access to cheaper financing existing in Chile between different sizes of companies. Large companies can issue bonds, and have captured from Chilean sources (coming from pension funds) a figure close to USD5 billion in financing at low market rates since 1990 to 2009. Similarly, the Chilean tax system has contributed to large corporations, financing them to zero-cost up to 92% of the USD54,000 million comprising the "Taxable Profits Fund" (in Spanish FUT), which is the sum of the tax exemptions that the Chilean state has granted to the national companies in the period under study 1990-2009 (SII, 2013).

184 The argument stressing the need for deep reforms possesses a potential applicability in countries in which the introduction of a neoliberal model produced moderate opening and a limited market liberalization, but is not applicable in the Chilean case, in which both processes were extremely radical and unrestricted.

Chile has not been successful in inducing productive diversification to areas of higher added value and a clear orientation to external markets in all sectors and company sizes (Claro, 2017). The presence of increasing market concentration and the political and economic power of the larger Chilean corporations has deep institutional roots.

Our findings related to depth of process of economic concentration are coincident with findings of other related research. Dissimilar literature about the deployment of the Chilean Model, shows that trade openness has been accompanied by a severe process of economic concentration (Fazio, 1997; Sapelli, 2002; Agosín and Pastén, 2003).[185]

In spite of this evidence, in several of these studies there was not a clear diagnosis as to whether these phenomena were inevitable or not and if it is possible to develop the Chilean economy without this type of economic concentration.

In addition, our analysis of that issue suggests that such concentration has eroded the productivity of the economy in a way analogous to that described in similar contexts in the literature (Cavalcanti and Facchini 2005; Okubo, 2009; Facchini, Namini et. al. 2012). For this reason, our research will attempt to provide evidence of this trend by evaluating the relationship between economic concentration and productivity.

185 In the literature about Chile, many analysts accept the fact that weighty market concentration has accompanied the trade opening of the economy. Authors like Fazio (op. cit.) postulated, from an orthodox Marxist standpoint, that economic opening would have been essentially a deliberate strategy for the generation of economic concentration in all areas. Other authors like Sapelli (op. cit.), from a clearly neoliberal perspective, acknowledge the high levels of concentration produced by trade liberalisation, but argue that this situation only expresses the greater relative efficiency of large firms. Given the trade openness, these firms lack real market power; they are permanently threatened by potential competition from imported substitutes. Agosín and Pastén (op. cit.), focusing only on the concentration of large companies listed on the stock exchange, declare which: "*The Chilean system of corporate governance is a typical example of the "insider variety". Its main problem is the conflict of interest that arises in such systems between controllers, usually a large group, and outside interests, normally AFPs (private pension funds), national and foreign mutual funds, insurance companies, holders of ADRs, and individuals".* Based on their analysis, they place their focus on the negative effects of some specific forms of corporate governance and on the modalities of the distribution of property and profits of Chilean corporations as one of the main channels that produces ownership concentration.

5.16. The Studies about the TFP made in Chile

The relationship between openness and total factor productivity is a widely-studied issue, especially in the Chilean case, in which it is a subject of high political relevance.

Various academic studies have tried to explain the evolution of the TFP of the Chilean economy in such a way that, it has been quite established, as a general conclusion, that trade liberalization and liberalizing economic policies seem to contribute to a certain growth of the aggregate TFP in the golden years "of the Chilean economy, but which did not therefore achieve a sustained growth path of this after 1997, TFP has not recovered the positive trend observed before the Asian crisis (Figure 5.8).

Regarding the fall of TFP during the period 1998 and 2009, several studies carried out in Chile grouped their causes in different ways. For example, Magendzo and Villena (2012) divide these causes into a group of causes considered external to the Chilean economy; and in another group, that obey to internal factors, especially those associated with the lack of adequate public policies. In the first group, they include the rising cost of energy, the Asian crisis and the copper boom associated with the real exchange rate.

The second group includes the microeconomic inflexibility, the scarcity of adequate human capital, the increase in logistical costs, the lack of competition in the markets, the scarcity of social capital, the deficient investment in research and development and the volatility of the exchange rate. Other authors (e.g. Fuentes, 2011), from a strictly neoliberal perspective, consider that the reduction in the growth rate of post-1997 TFP is mainly due to the low microeconomic flexibility to face negative shocks, as happened with the Asian crisis, which raised production costs.

This low flexibility is manifested, accord his view, in the existing restrictions to efficient labour adjustments, while the negative shocks over the economy, had been produced by the imbricate influence of the increase in the minimum wage (from the end of dictatorship onwards), the impact of the Asian crisis (1998) and by the rise in energy prices (2004).

The comparison of the findings of those research's that use parametric methods, with those studies that use non-parametric methods, shows similarities and differences. A similarity is that they all find average annual rates of negative growth of the TFP

(although of different magnitude) in the respective periods. But some research's find drastic changes in the growth rate between one year and another (from negative to positive and vice versa), while others find a more stable, negative and decreasing change in all years.[186]

The work of Magendzo and Villena (2012), the only ones who analyse a similar and comparable period (1992-2010), find highly negative growth rates of -15%, -9% and -7% in some years, followed by positive rates. An important point of discussion is the relative importance of energy in the manufacturing industry and its possible effect on the decrease of the TFP of the sector.

Álvarez et al. (2008), Echavarría et al. (2008) and Blümel et al. (2010), analyse the relationship between the variations of the TFP and the changes in energy prices in Chile. Álvarez uses data from the industrial sector at the plant level to analyse the relationship between price of energy and labour productivity in Chilean manufacturing, and estimate that the energy shock of the first years of the 2000s (due to the increase in the price of the oil and the decrease of water to generate electric power), explain between 20% and 60% of the reduction of its productivity in the period 2000-2005, and a loss of 0.5% of TFP in those years at the aggregate level. They also find that the most energy-intensive sectors have experienced the greatest reduction in the rate of productivity growth. The results of Magendzo and Villena (2012) and Fuentes (2011) has been confirmed by Caballero et al. (2004), Beyer and Vergara (2002), and Álvarez and Fuentes (2011).

In our opinion, it makes no sense in our analysis to replicate, for the period of analisys 1990-2009, the well-known and widely discussed TFP estimates made by other authors.

186 All the studies for the period 1998-2010, indicate that the TFP decreased significantly, and in general reject (by lack or weakness of evidence) the hypothesis, of neoliberal origin, that sustain which, this reduction is due to the negative technological change, while the technical efficiency remains constant. The rejection of that working hypothesis, formerly extracted used a parametric approach, has been based in findings of studies that utilise nonparametric methods for the TFP estimation and analysis (Candia et al., 2016) and, which, given the differences with the results of the parametric methods, allows to make comparisons that have made it possible to obtain new conclusions. On the other hand, the non-parametric approaches, severely questions the likelihood of the neoliberal hypothesis, since they find that, parallel to trade openness, it is not observed in the Chilean economy, the presence of new higher levels of technical efficiency.

Moreover, the data available in Chile makes it difficult to move forward of such estimates, because it is beyond the reach of independent researchers to build balanced panels at the company level, in order to control the effects of replacing them. In addition, there is no possibility of building an adequate deflator (such as the producer price index, PPI) for the entire period studied here.

Although the INE publishes an IPP for the entire economy and one for manufacturing, these are only available since 2003 and 2009 respectively. The important thing is to be able to affirm that, the evidence reported by diverse and not questioned studies (including several studies developed by researchers of clear neoliberal orientation, e.g., Schmidt-Hebbel, 2006) show an undeniable fact: the TFP of Chile was, in 2009, only slowly superior to that which the country had in 1960, during the boom of the import substitution model.

Certainly, different arguments can be used to explain this. The low quality of the available data, which does not allow for the sophistication in disaggregation by quality of the factors of production; the low sectoral disaggregation of the available data, which limits the TFP estimates for the same reason; the influence of the external shocks that the Chilean economy has faced, a fact which is a strange argument for the supporters of the unrestricted opening of the economy. Finally, it is argued, by various authors already quoted, that a crucial factor is the negative role played by the new post-dictatorial governments, which would have "altered the normal functioning of the labour market", increasing the monthly basic salary from 170 USD in 1990 to 311 USD in 2009.

Figure 5.8. Evolution of GDP, APL and TFP: 1960–2009
Source: Author´s elaboration based on figures from INE and Central Bank, (2010).

In our view, the weakness of the process of technological diffusion across the Chilean economy seem to be clear because all available data show that Chilean model has not produced the expected increase of total factor productivity (TFP) in the economy as a whole. The TFP is virtually stagnant and exceeds, only in a small percentage, the level that the Chilean economy had in 1960. Nevertheless, the sources of this trend are beyond the period of our analysis, therefore analysing the source of this stagnation is not possible without a wider perspective that made necessary to observe Chilean economy evolution at least from 1960 to 2009.

In Figure 5.8. (in the Graph on the left side) we can see evolution of Real GDP, Average Labour Productivity and Total Factor Productivity, between 1960 and 2009. There, it is possible to observe the growing Gap between GDP and productivity growth; however, in Figure 5.8. (in the graph of the right side) it is possible to observe in a more detailed form the evolution of the gap between average productivity of labour and multifactorial productivity growth.

It is well known that traditional measures of productivity, such as Average Productivity of Labour, are focused only on one input – labour – and take account only of the volume

of hours worked and not changes in the composition of factors of production over time. On the other hand, TFP captures the efficiency with which capital and labour are combined to generate output. This process of "technique´s selection" (K/L) depends not only on business' ability to innovate, but also on the extent to which they operate in an institutional, regulatory, and legal environment that fosters competition, removes unnecessary administrative burden, provides a modern and efficient infrastructure, and allows easy access to finance (Syverson, 2011).

During the period 1960 to 1973, both productivities have been virtually deadlocked, and the GDP moves very little above productivity. The growth of GDP and productivity was not prominent in this period. After the low productivity of the 1960s, the three-year period of the "Unidad Popular" brought with it a collapse of productivity and production and it began to recover significantly only after the implementation of the neoliberal model. In fact, after the coup of 1973 and the economic opening that began in 1976, we can observe some changes in the dynamics of growth of the GDP. Thereafter these changes do not conform a regular tendency and the incipient level of growth, was uninterrupted by the financial the crisis 1979-1982 produced by rigid application of the monetarist approach. The introduction of measures of rectification of the old monetarist model from 1982-1984, lets than the Chilean economy begins a golden decade 1985-1995) growing at annual rates by above their historical levels.

In spite of this, does this situation justify claiming that neoliberal policy induced a "giant productive jump" in the country?

If strong GDP growth means "giant productive jump", indeed Chile did achieve this. However, the term is not appropriate, because the growth of production was achieved alongside significant productivity stagnation and therefore was the result of an intensively extractive model, not founded on productivity and therefore is barely sustainable.

It makes more sense to refer to this phenomenon as a "production jump", since the term "productive" brings associated a mix of growth of production and the ability to produce, (i.e. productivity), which is not observed in this case. In general, we can assess, based on the abundant evidence reported in this chapter, that the development of the neoliberal model has not been accompanied by significant jumps in productivity of the Chilean economy.

As display Figures 5,8 (left side) and 5.8 (right side) throughout the period that mediated between the start of the trade openness and the temporary reversal of this (1976–1982), both productivities exhibit a slowly build-up; however, the TFP moves above the APL, suggesting the presence of incorporation of the same degree of technical progress to the Chilean economy as during the first phase of the process of opening. However, the financial crisis of 1979–1982 caused product and productivity to collapse and only after the reforms that gave rise to the "Second Chilean Miracle" (1984) did the country recover a path of output growth followed by some improvement in productivity. Despite this, the dictatorship ends with both productivities (average and multifactor productivity) at lower levels than in 1960 (Ministry of Finances, 2015).

Figures 5,8, also reveals that, between 1990 and 2009, both productivities grow in a continuous way, however, TFP growth sits steadily above APL, at least until 2008. From that year onwards, the growth process become increasingly extractive, that means based on the intensive use of factors and not on technical progress; the TFP growth rate falls under that of APL and subsequent to this, both product growth and productivity growth deteriorate strongly.

In the decade following 2000, GDP per capita growth slowed to less than half the pace of growth during the "golden period". Towards the end of the first decade of the present century, per capita GDP was almost two-thirds lower than in advanced OECD member countries (OECD, 2011c) and the aforementioned fall in productivity showed a scenario becoming increasingly difficult to overcome.

The stagnation of productivity has become particularly acute since 1998, preventing Chile from faster growth over recent decades. It seems that there are powerful institutional factors preventing greater productivity growth. As it is recorded in Figure 5.9. built using official estimates, total factor´s productivity (TFP) from 1960 to 2009, only has increased around 20%.

The behaviour of Chile's TFP has been especially puzzling since 1997 onwards. Given the strong integration of Chile within the global economy, the deceleration of the post-1997 productivity growth was deployed simultaneously to the Asian crisis 1996–1998. It could be conjectured that; the productivity drop was associated with the fall in the investment rates of that period.

Indeed, during the period between those two years, the Chilean investment rates decreased, especially when they are compared to those at the beginning of the decade. However, since 2004, the investment rate has had a remarkable recovery but the measured productivity growth remains low (BCH, 2006, 2012). The slowdown in productivity in Chile is difficult to explain because it coincides with a marked increase in investment in machinery and equipment which, as a percentage of GDP, has almost doubled since 2004, and since the end of 2008, represented about 50% of the total investment (op. cit.).

The previously cited studies in general coincide with the evolution of productivity of the Chilean economy between 1990 and 2009.[187] All that shows that the TFP growth has been systematically falling since the nineties. The explanations of this situation reported in these studies show that the increase in the TFP of the golden period of the Chilean economy has been systematically reduced as a result of several factors. In first place, it is necessary mention that the increase in energy prices imply that part of the stock of capital that was acquired for a situation of low prices, was underutilized. A fact which indirectly affected productivity in various sectors of the economy.

In second place, it is frequently mentioned that the direct effect on the TFP exercised by the reduction of the added value of the electricity sector (caused by the fall of hydroelectric generation and its replacement by more expensive sources (e.g. coal, oil and gas). In third place, the fall in the copper ore grades and the effect of water scarcity on the added value of the mining sector, are pointed out by the industry as factors of significant importance.

There are also opinions that blame the fall in the innovation rates of the cooper companies (which in reported in the innovation surveys), and the stagnation of the process of export diversification of goods and services. However, the fall in productivity has been maintained in the presence of the fall in the price of energy resulting from the massive generation of solar energy and the greater regulation of the energy sector. Additionally, it can also be pointed out that the scarcity of groundwater has begun to be slowly replaced by mining companies with de-salinized water.

187 The most accurate estimate of the TFP available for our period of study, is that carried out by Magendzo (op.cit) who estimates that, in the period 93-98, the growth of the TFP was 2.6% per year, compared with 1.2% in the period 2000-2008 and 0.6% between 2010 and 2012.

However, it is not often that the neoliberal analysis emphasizes the relevance of these last factors, whose presence definitely does not fit in the description that the model's supporters make about its success.

Magendzo and Villena (op.cit) perform an analysis of the evolution of TFP growth excluding the effect of changes in the energy matrix and the deterioration in the quality of copper deposits. Using that data, depurated by the exclusion of the mining, electricity and gas sector, it is possible to observe that the TFP in the period of 93-98 grows by 1.7%; then increases to 2.5% in 2000-2008; and falls slightly to 2.3% in 2010-12. In other words, the changes introduced do not alter the evolutionary trend of the TFP, but show that the most dynamic sectors of the Chilean economy, intensive in the exploitation of natural resources, are far from providing productive dynamism to the economy and are a factor in depressing the absolute values of this. On the other hand, the most dynamic sectors such as forestry and fishing, regardless of the benefits that economic opening is expected to bring to their productivity, do not show during the twenty years analyzed a development of their productivity that can be defined as significant.

That is, when excluding from the TFP estimates of the factors that are not related to efficiency, but rather to the availability of natural resources, it is possible to conclude that the exceptional result of the so-called golden age, is consistent with the fact that copper deposits were being exploited at higher ore-grade of the minerals, and there was access to cheap energy and water because at that time the energy matrix was more hydric.

To these factors, we can add that the Chilean national accounts do not include in their GDP estimations environmental issues, ecological deterioration, overexploitation of fisheries, over-density of salmon production in the austral zone, or deterioration of soil quality and destruction of biodiversity produced by plantations of large forest corporations, that are using a continuous surface equivalent to 70% of The Netherlands territory.

Once Chile exhausted its "easy" extractive phase, the measurement of TFP growth, even without incorporating the stock of natural resources, deteriorated significantly. A fact which suggests a certain impotence of the trade openness to allocate the resources of the economy in such a way that can move forward the growth of GDP and productivity.

According to the OECD (2011a:54), the diminished contribution of labour explains about a third of the reduction in the Chile´s GDP growth in the past decade, and the visible stagnation of TFP the remaining two thirds. In relation to this, OECD (2011a) has emphasised the presence of low levels of competition in the market of products as a hypothetical cause. OECD measurements of market competition levels using margins of price/costs suggest that market competition in Chile is quite below OECD standards. This would seem to confirm our findings relating to the presence of strong oligopolistic powers operating in those markets, as we have previously identified.

When analysing this issue, other authors such as Bitrán and González (2010:13) emphasise the normative area, indicating that having maintained TFP rates prior to 1998, the country should have embarked on a process of structural reforms with the aim of enhancing productive diversification and sophistication. However, contrary to the trend shown by other countries, Chile did make a serious effort in that direction but, innovation and productivity decreased considerably.[188] Independent of differences in diagnosis, Chile´s economic growth fell from above 7.5% annually in the period 1986–1989, 7.7% the period 1990–1997 and less than a half of that level in 1998–2009 (3.3%) (op. cit.).

The breakdown of these variations in economic growth shows that the contribution to the growth of capital has remained stable in both periods and the contribution of labour fell a point. The greatest reduction corresponds to TFP, which reduced its contribution from 3.05% in 1986–1997, to a level of – 0.35%, in 1998–2009 (OECD, 2010).[189]

Chilean TFP has increased only about 1.3% annually in the last twenty years (1990–2009) just exceeding 20 points above the productivity level that the country had in

188 This critical view of public policies oriented to innovation and productivity, on the part of Eduardo Bitrán (2010), is quite unusual since these policies were under his direction during all of the third "Concertación" Government and they currently continue under his responsibility during the fifth Government of that coalition. Although the limited outcomes of such policies are well known, they have continued unaltered from 1998 to the present date.

189 In the last three decades, the OECD TFP gains average between 1% and 2% per year, contributing TFP of more than 50% of the total growth in those countries (OECD, 2010). Moreover, countries that have been able to make the transition have maintained TFP growth rates higher than 1.5% per year for long periods and in a constant way.

1991, which was the same level that the country had during the period of import-substitution, half a century ago (1960).[190]

However, factor remunerations have moved far above it, oriented more by GDP growth. In spite of this, as can be seen in Figure 5.9, the aforementioned remunerations have moved somewhat erratically, in relation to variations in multifactor productivity.

Looking in an isolated way of the evolution of the TFP, using the information provided by the National Accounts of Chile published periodically by the Central Bank, it is observed that the remuneration of capital (eg, the operating surplus) has a strong upward trend only interrupted by the Asian crisis that began in 1997 and the subprime crisis that began ten years later.

After both events, without significant increases in the TFP, the remuneration to the capital increases its weight within the GDP, while the opposite happens with the remuneration to labour; after the end of the subprime crisis, it was still incapacitated to recover its levels prior to the Asian crisis.

190 http://www.dipres.gob.cl/594/articles-105498_doc_pdf.pdf

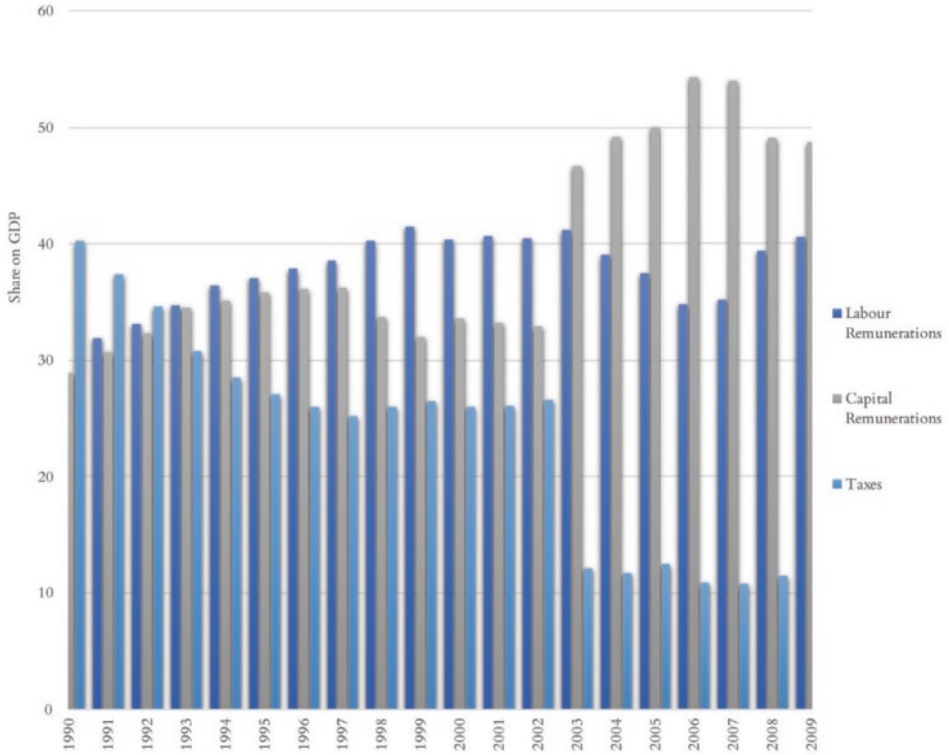

Figure 5.9. Productive Factor´s Remuneration
Source: BCCH, National Accounts 1990–2009.

This is a contradictory situation in respect to the forecasts given by neoclassical economic theory[191], considering that from 1973 onwards Chile exhibited a period of greater trade openness and market liberalisation than has ever been registered in the country throughout its history.

If these levels of opening have not been able to generate a relevant If these levels of opening have not been able to generate a relevant synchrony between the evolution of the Productivity of the factors and their remunerations, that can only mean that they have not managed to settle in Chile, new processes of resource allocation able to improve the multifactor productivity of the economy. Then, the whole of neoclassical explanation comes into question (Klenow and Rodríguez-Clare, 1997).

191 In addition to this factor, OECD reports that the presence in Chilean markets of institutional arrangements *"discourage the entry and exit of firms, disheartening entrepreneurial risk-taking and diversification into new activities of higher productivity".*

This problem is seen even more clearly in Figure 5.10. in which GDP growth trends are plotted, vis a vis the evolution of the TFP and the remuneration of capital.

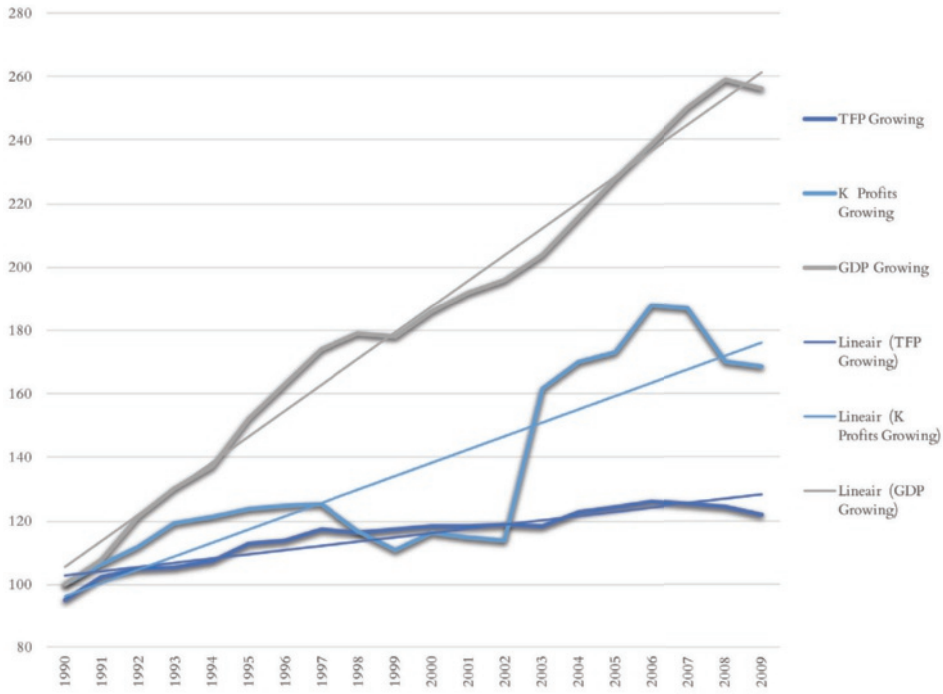

Figure 5.10. Evolution of TFP, GDP and Capital Profits Growth.
Source: BCCH, National Accounts 1990-2009.

This table clearly shows that, while in the two decades analysed, real GDP is close to 300% accumulated growth, capital remunerations are approaching 200% in the same period, growth that can only be seen interrupted by the effect of the two external crises mentioned above. However, the evolution of the TFP is very weak, reaching only 20% during the aforementioned period.

All the above, seems to indicate that the growth of the Chilean economy is not based on the growth of productivity and that the remunerations to the capital either. On the contrary, the information in the previous table suggests that, in addition, the profits of companies are associated with the market power they have managed to consolidate and that, therefore, only the presence of shocks in external demand manage to stop its evolution. The positive effects of openness on productivity are likely to exist at

the sectoral or subsectoral level, however, if so, its magnitude is not of such a size as to be able to impose itself, at the level of large numbers, on the set of the economy.

During the twenty years analysed, the Chilean economy shows growth without productivity and with high capital gains, something very different from the results that the neoliberal model promised would be obtained in Chile, in the event of implementing its policy recipes.

5.17. Conclusions

Throughout this chapter, we have reported how the neoliberal hypotheses is not related with the real way in which trade openness has actually operated. The reason for this lack of alignment between the hypothesis and reality reveals a series of errors in the expectations of the neoliberal thesis in relation to the effects which trade openness should induce in the system of relative prices and therefore on the efficiency of resource allocation mechanisms.

- The falsified hypothesis sustained that when an economy is equipped with an adequate macroeconomic environment and a free pricing mechanism, efficient resources allocation mechanism would be assured. Based on this, the trade openness and liberalization of Chilean economy, which has been accompanied by various macroeconomic policies that have kept the fiscal accounts healthy, controlled the balance of payments and relatively dominated the exchange rate, would generate the reallocation of its factors of production (capital and labour) from its most backward toward the more productive and globalised sectors, improving the general efficiency and productivity of the economy.
- However, our findings show that the problems of neoliberal model are not only related to withdrawn issues, like the speed in the achievement of proposed outcomes, or in the variability of the growth process. From our research is possible to conclude that trade openness has not been able to install an efficient price system in the Chilean economy. The relative prices of the Chilean economy are markedly misaligned with the evolution of international prices. This occurs in a discrete way in the sector of tradable goods, but in a strong manner in the non-tradable sector. A sector in which Chile shows prices of electricity, drinking water, real estate, banking services and in various other

economic sectors, that far exceed the evolution of these prices as observed in the markets of Chile´s main trading partners.

- The price relationship between tradable and non-tradable goods displayed by Chile´s economy, gives the impression of complying with the market power of companies that exhibit higher price levels and does not correspond to the eventual rise on income of individuals and families, resulting from the increase in GDP pc of the economy.
- Regardless of the unquestionable increase in GDP pc of the Chilean economy (a figure that is highly praised by international financing agencies, especially WB and IMF), it should be considered that when these "impressive" figures are disaggregated and distributed, the average income of the 75% of Chilean families do not exceed 1800 euros per month and 50% of them do not exceed 750 euros per month.
- Measured in dollars of 2010, at ppp, the GDP pc of Chile in 1990 was of US $ 7,164,754 and in 2009 of US $ 9,230,542. That means that the GDP pc increased in that period in 2,065,788 dollars annually. Of these amounts, in 1990, 62.41% was destined to the consumption of people, while in 2009 that percentage had fallen to 58.78% (WB, 2010). The above means that, over twenty years, the per capita consumption of the population of Chile has increased by only US $ 981 per year, that is to say in three USD per day. This is a figure that, even while assuming that this amount was distributed in a perfectly egalitarian way, it would have changed the preferences of people's consumption, diverted their demand, from the area of tradable goods (eg clothing, food, machinery, etc.), to the area of non-tradable goods (e.g. financial services, home purchases, personal services, etc.), explaining in this way the unpredictable evolution of the CPI of the economy
- The neoliberal approach to development focus its expectations on the impact that trade and market liberalisation must exert in open economies by means of process of technological diffusion induced by the so-called 'technological catch-up' effect that would carry out the reallocation of resources between sectors. This approach assumes that it is cheaper to imitate existing technology than innovate. In this way, the most backward sectors of an economy such as the Chilean one, could benefit from their relative backwardness and catch-up using technology from the more advanced countries, inducing convergence with the most developed economies. However, the data analysed in this chapter lets us conclude that the technical progress diffusion mechanisms are not operating in that way basically because Chile´s trade openness has not been

able to implement a pricing system with the functionalities promised by the neoliberal model, and the implementation of the neoliberal model has not shown a greater contribution in the area of the establishment of economic growth supported by productivity.

- The reasons why this has not happened over the 40 years of neoliberal policies can be the subject of multiple approaches and discussions; however, the undeniable fact is that the TFP has not increased in Chile in a parallel way to the trade openness. The price system does not show to be immune to the effects of economic concentration, nor did it make possible the existence of a new resource allocation system which, in the neoliberal discourse, is ever associated with the new relative prices. Then, trade openness does not show significant effects in the productivity of the sectors of the economy that develop non-extractive activities. Moreover, even while it happens in some sectors, during small periods, these productivity developments do not show permanent effects either.

On that basis, we must conclude that:

- Chile´s Domestic prices, 40 years after the starting point of trade openness, are not yet synchronised to international prices as expected. Domestic prices are not converging to international prices. On the contrary, they tend to maintain a permanent misalignment in relation to international prices.
- Although during the period analysed, we can observe an important long-term decline in inflation, this decrease has not been enough and inflation values tend to exceed the parameters defined by the Central Bank of Chile as desirable. If we observe the behaviour of inflation from 2009 onwards, it is clear that the adjustment of domestic prices to international ones, is far from being consolidated. The absolute value of the domestic inflation exceeds the inflation rate of the main trading partners of Chile, since domestic prices are moving across the relevant international prices for Chile.
- In the Chilean economy, the prices of non-tradable goods exhibit bigger increments than tradable goods. The explanation of these state of affairs, seems to be related to the non-competitive market structure of non-tradable goods. The low and decreasing level of tariffs of the Chilean economy, present high and increasing levels of economic intra-sectorial concentration in practically all industries, and also show, at an inter-sectorial level, unacceptable levels of concentration.

- The Chilean economy additionally shows a low level of pass-through; independently of its fully openness, devaluations or revaluations of the exchange rate are not transferred to domestic prices, even closely to a one-to-one relationship. The most reliable explanation of this process is related to the non-competitive structure of the Chilean markets, which, despite the radical process of liberalisation, has granted substantial and asymmetric market power to a small segment of large enterprises.
- We have not only shown that the price elasticity of aggregate demand in the Chilean economy is quite low, but we have also demonstrated that such elasticity has declined markedly over time. The explanation for this behaviour, which is unusual for a fully open economy, lies in the behaviour of the non-tradable goods sector. We have shown that non-tradable is a sector that has gained importance within the basket of goods used to estimate ICPI. We have also shown that this process is due, to some extent, to the increase of GDP per capita in the country. However, the influence of non-tradables on inflation is an issue essentially related to the presence of high market powers.
- The high inelasticity of demand in which large Chilean firms are operating produces high levels of rent-capture from the side of large firms with high market power. As a result, LSE can obtain a high control of aggregated and sectorial demand.
- A combination of these factors seems to be the reason for the low capability of the Chilean economy to transmit technical progress in the productive fabric. An economy like the Chilean one, in which trade openness is translated into an increasing market share of large firms, a sustained fall in price´s demand elasticity and in which market`s presence of non-incumbent firms tends to decline, is acting "contrario-sensu" of predictions made by neoliberal advocates of the Chilean model.
- If the evolution of relative prices of the Chilean economy do not adjust to progression of international inflation, then the system of relative prices is altered as a whole. Given that It does not set up price efficiency, the impact of the openness is not being transmitted to the productive fabric, and economic resources tend to be assigned more on function of the market power of large companies than based on economic efficiency reasons. This situation not only affects the absolute pricing level, but also essentially affects the system of relative prices between tradable and non-tradable goods, as long as each type of goods uses inputs from the other sector.

- The presence of LSE meaningful market powers seem to be associated to differential of inflation induced by the upward mobility of the prices of tradable goods and rigidities of non-tradable goods prices. This situation may be explained by the fact that large oligopolistic companies operating in the non-tradable sector are working in segments of highly inelastic demand curve, developing a market power that allows them to define a mark-up. This lets them raise their prices beyond the limits defined by trade openness, preventing a complete transmission of international prices.
- If the prices resulting from trade openness and liberalisation only reflect the market power of large enterprises and not the marginal cost predominating in foreign markets, it is clear the absence of a spot-on pricing system like the forecasted by neoliberal. Because that, the Chilean economy seems to be experiencing a negative trade-off between growth and productivity, a growing of the amount of resources allocated towards the commodity-intensive sectors (based on natural resources) and a decline of sectors relevance of sectors of high productivity and technological complexity.
- The changes in relative prices have failed to alter the resource allocation processes in a progressive way; they are increasing rather than reducing the existing technological heterogeneity among sectors and sizes of enterprises. We cannot find relevant evidence which show that a clearly efficient system of resource allocation has been installed in the Chilean economy. The non-presence of that mechanism is the key explanation for the low total factor productivity of the Chilean economy who express the fact that, Chile´s economy has not benefiting from the raising process of neoliberal market liberalisation, at least in the way that neoliberals promised.
- In this chapter we have showed that, the neoliberal hypothesis regarding technical progress diffusion, exhibits assumptions and made forecasts about the agent´s economic behaviour that clash empirically with the Chilean reality. Additionally, it is quite clear that the positive outcomes forecast upon the implementation of the neoliberal model of development have not been accomplished and that the country has only consolidated an extractive economic model.
- In sum, we can conclude that the promises of the neoliberal model have failed and, at least in the areas analysed in this chapter, their optimistic goals have not been achieved. We think that rather than fulfil their promises, the neoliberal prescriptions have tended to promote an institutional agenda that tries to consolidate a new economic order not necessarily tied to their old promises.

The neoliberal discourse associates the policy measures implemented by them with the positives attributes that perfect competition markets theoretically have. However, the outcomes actually produced by the Chilean model are very different to those promoted by neoliberal proposals. This last conclusion will be deeply analysed in Chapter VIII.

Chapter 6

Trade Openness, Poverty and Income Distribution

The objective of this chapter is to analyse the issues related to the behaviour of the Chilean triangle: Growth, Poverty and Inequality, during the trade openness and liberalisation period under analysis (1990-2009). Because that, here our focus is primarily oriented towards the falsification of the research hypothesis in the area of income distribution which sustains that: *a reallocation of the factors of production (capital and labour), from its most backward toward the more productive and globalised sector of the economy would result in labour of upgraded productivity, thus creating higher remunerations and improving domestic income distribution*.

In order to falsify that hypothesis, in this chapter we analyse if actually, trade openness and market liberalisation has been related to presence of a greater income equality or, on the contrary, to a bigger income inequality

In order to analyse that issue, we investigate the anatomy of income distribution in Chile: 1990-2009, the evolution of the distribution of monetary and non-monetary incomes, the impact of social spending on income distribution and the relationships between poverty and specific institutional arrangements in the Chilean labour market.

6.1. Growth first, Distribution later

From several sides of the economic theory, it has been assumed that "development" is a mix of economic growth and income distribution (Lucas, 1988; Aghion and Bolton, 1997). It is because of these reasons, which, some authors consider that the first objective of any developmental policy is to generate a dynamic enabling growth, and in a second phase, promote an income redistribution process that enforces equality, without limiting economic growth (Kuznets, 1957; Fishlow, 1995).

The neoliberal point is associated with the understanding of development as a rigid sequence of events. Firstly, trade openness will generate improvements in the allocation of resources driven by new relative prices. The outcome of this process is that labour of higher productivity, that should be remunerated with higher wages, positively impacting the primary distribution of income. From this believe is assumed that the income distribution will tend to increase together with the GDP and the productivity of the economy framed on a trickle-down behaviour. Firstly, the income of the richest population deciles grow up and secondly, the workers' income also grows. Such increases will be poured out from the top of income towards the sectors most deprived, improving so, gradually the distribution of income.[193]

193 The various components of our work hypothesis are made up of a choice of analyses carried out by Chilean political and academic leaders, who recognize ranks in neoliberal thinking predominant in Chile. (J. Piñera, 1978, Corvo, 1985, Álvarez and Fuentes, 2003, Álvarez 1999, Buchi, 2008, 2009, Larraín and Vergara 2009b, Larraín 2012, Morande and Vergara 1997, Schmidt Hebbel, 2006 have been extremely explicit in the defence of that point of view and its associated projections Some others have limited themselves to defending somewhat more limited projections, which nonetheless converge in a single and positive vision of the future after the neoliberal reforms. The presumption that assumes that Chile will be a developed country before 2030, has been consistently defended by the Chilean Minister of Foreign Affairs (2010-2014) Alfredo. Moreno, https://elpais.com/internacional/2011/03/09/actualidad/1299625211_850215.html. The presumption that assumes that Chile will converge to the product and productivity of the OECD in the coming decades, has been defended by the President of the Republic Sebastián Piñera (2010-2014, 2018-2022): "Our mission is that by 2025 Chile will be a developed country, without poverty ": http://www.cooperativa.cl/noticias/pais/sebastian-pinera/pinera-nuestra-mision-es-que-al-ano-2025-chile-sea-un-pais/ 2017-10-18 / 114443.html. The presumption that assumes that poverty in Chile will disappear in the same period as a function of GDP growth has been defended by: Moreno Ibid; Paulina Henoch and Juan Ramón Larraín (2016), "The role of economic growth in poverty reduction". Report 154, Freedom and Development. The presumption that equal opportunities will be permanently installed in Chile has been defended by prominent neoliberal academics from the Pontificia Universidad Católica de Chile (Ibañez and Lüders 1983). The presumptions that assumes that, after the opening, production resources would be allocated efficiently were raised from the Central Bank of Chile (De la Cuadra, 1973). The presumption that assumes that in Chile, after the opening, the remunerations of Chilean workers will converge towards the average productivity of labour, thus

The presence of this trickle-down strategy (Adelman & Robinson, 1989)[194] constitutes the grounds of neoliberal policies of income distribution associated with the Chilean model. In fact, that strategy contained in the neoliberal hypothesis, sustains which, without the intervention of any other agents and relying only on the action of free markets, the economy can obtain an adequate income´s redistribution (Schultz, 1981; Valdes, 1999; Lodáres 2014).

As we have discussed in the previous chapters, the institutional environment and the institutional arrangements affecting the operation of the Chilean economy, are promoting a concentrated accumulation of capital on large companies that control the main markets. Therefore, it is highly possible that growth processes are not being conducive to social progress, but just acting as driving force of the profit´s concentration in those economic agents that have control of the markets arrangements.

When factorial incomes´ distribution strengthens a concentration´s dynamic, the most probable scenario would be embracing of a worsening´s path of the regressive income distribution prevalent in the Chilean economy. The neoliberal view, which neglect the dynamic formerly described, is contained in the central working hypothesis of this research; nevertheless, it still has not been explored empirically. For that reason, our intention in this chapter is to develop a full process of falsification of that hypothesis that let us to demonstrate the plausibility of neoliberal hypothesis or, on the contrary, show that others factors, different than trade openness, are explaining in a best way the real impact exerted by trade openness upon on the distribution of income.

improving the distribution of income, appears in the document that played the role of the first stone of the neoliberal model (El Ladrillo, 1973), and in the paper by José Piñera: "Chile to the first world: a liberal agenda for the last section" (1973). Each of these neo-liberal presumptions has been widely disseminated in Chile and around the world, being exposed in great detail by various Chilean academics and politicians, of whom about twenty have been analyzed and included in the bibliographical references.

194 The idea behind that proposal was that economies would grow and wealth would trickle down from the rich to the poor. That theory assumed that when economic growth took off, the rich would spend more on luxury goods, creating jobs for the non-rich. The non-rich would then have more to spend, which might create new jobs in, for example, the construction sector as they could afford better housing. Thus, as long as there is economic growth, the wealth of the rich trickles slowly down to the non-rich and to an emerging middle.

6.2. Growth, Poverty and Inequality

The Chilean champions of the neoliberal model have argued that the modality of growth associated with their prescriptions is definitely "pro-poor".[195] This proposal assumed that trade openness would have established new rules of the economic game which has being producing high growth rates in Chile, and a process of high elasticity of poverty reduction in relation to growth, in such a way that would have consolidated a national growth pattern tending to reduce poverty (Henoch y Larraín, 2015; Libertad y Desarrollo, 2015).

Obviously if this trend of poverty reduction had an endogenous and permanent character, funded in a specific institutional environment and in neoliberal institutional arrangements, in the long run it would be reasonable to expect, as a result, a sustained improvement in the situation of the poor. We should also expect a permanent rise in the percentage of the population placed above the line of poverty and therefore a progressive trend in the distribution of the gains of economic growth.

If we use neo institutional approach of O. E. Williamson (1996) to analyse that issues, result crucial the quoted distinction between governance structures, formalised agreements and contractual arrangements (e.g. micro-level relationships that are established among different economic and business actors) and institutional environment.

The institutional environment defines the primacy of regulatory institutions, normative institutions and cognitive institutions in influencing the legitimacy of economic activities and the way in which these institutions might influence economic and business relationships. In the Chilean case, the main rules of the game, at the macro-level, that defined the institutional environment are six:

1. The Constitution of 1980, which is essentially an economic Constitution.
2. The principle of subsidiary State, which prevents any action of the State in the economy in case that such action, may be developed by the private sector.

195 More than 20 years before the elaboration of the well know definition of Ravaillon and Chen (2003) as to "pro-poor growth", some Chilean neoliberal economists had elaborated a slightly restricted version of the same concept. From the middle seventies, they assess that pro-poor growth was one in which the amount of people whose incomes are below some previously established "poverty line" decrease as a share of total population (Katz, 1979).

3. The presence of super parliamentary quorums required so that the State can create new public companies or compete with those that were privatized during the dictatorship.
4. The autonomy of the Central Bank, which leave the monetary and exchange rate policy outside the sphere of decisions of the Government-dependent economic authorities.
5. The presence of a structural deficit in public spending policy, whose limit is 3% of the budget and that leaves fiscal policy extremely tied to a conservative concept of public spending.
6. The presence of a constitutional court independent of political power, whose main action is in the economic field and which, can leave without effect any law passed by Congress if that court believes it violates the principles of the Constitution.

This set of rules of the game controlling the elaboration of rules and requirements, to which individual organizations must conform in order to receive legitimacy and support, are those who ultimately define the institutional environment.

On the other side, the Institutional arrangements may range from formal to informal, with varying degrees of authority, accountability, and responsibility for coordination, handover, and delivery. In the Chilean case, these institutional arrangements are simultaneously shaped at local, regional and national level and mutually influence each other within a framework of complex inter-linkages and strategic feedbacks. These institutional arrangements must be understood as the dynamic set of formal and informal regulations and networks which, are shaped by economic exchange, socio-cultural norms and political regime[196]

In our opinion, both institutional levels have been a powerful device to promote economic concentration and to expand the market power of a small but powerful group of large corporations operating in the Chilean markets. On the contrary to our point of view, the neoliberal vision declares that openness would produce higher levels of competition, tending to dissolve the economic concentration, or maintain it circumscribed to those areas in which, either the size of the market or assets specificity make it inevitable.

196 In a more general context, they also may provide welfare, identity, solidarity and sense of belonging to the economic and social actors, but, in this case we will not analyse this kind of issues.

In relation to our judgements, Chapters III and V analyse the presence a strong process of economic concentration running parallel to trade openness, however it is very difficult to discern if indeed, the concentration phenomena obeyed a plan predesigned by certain business groups that aspired to take control of the Chilean economy and whose concretion was made possible by the coup of 1973. It is possible that concentration and the bad income distribution were simply a necessary consequence (but not necessarily planned), of the establishment of rules of the game in which, political and economic power was distributed in a highly asymmetric way among the different agents. However, the most relevant element for our analysis is not to determine the intentionality associated with the implementation of the neoliberal model. But rather we will focus on the realization of an empirical review of neo-liberal statements related to income distribution, in order to falsify their predictions and associated prescriptions.

The focus of such validation should be put on the analysis of the specific institutional arrangements of the Chilean markets and their consequences on the distribution of income. That means to assess whether, compared to the influence of relative prices induced by the economic openness, there are other kind of factors (e.g. impacts of institutional variables) which are have been playing a positive or negative role and whether that factors have had any impact in the Chile´s patterns of economic growth. This task will be addressed in this chapter, which will deal largely with the behaviour shown, during the period under analysis, by evolution of the so called: Chilean triangle of Growth, Poverty and Inequality (Bourguignon, 2004),

In order to clarify this behaviour, in the course of the chapter we will firstly analyse the anatomy of income distribution in Chile from 1990 to 2009, emphasising the distribution issues associated with monetary and non-monetary incomes. Additionally, we will analyse the impact of social spending on income distribution and the relationships between poverty and specific institutional arrangements existent in the Chilean labour market.

Both analyses will focus on the influence that the institutional environment and institutional arrangements has been exerting on social policies implemented during the period 1990-2009, and on the success or failures of Chilean public policies in the areas of poverty and inequality reduction. Through such analysis, we will try to identify the relationships that have actually been established between efficiency and equality during the openness and liberalisation process. In doing this, we will try to

determine if inequality is exerting any effect on efficiency and, if that is true, discern in which specific way this impact is taking place.

This is an essential exercise in order to evaluate if the market forces triggered by trade openness have been producing a simultaneous reduction of poverty and inequality or, on the contrary, there are institutional factors (institutional environment and arrangements) behind those process, exerting influences in other directions.

6.3. The Theoretical Debate about Inequality and Economic Growth Trade-Off

The discussions about this trade-off are not a topic of mere local interest. Although this area of study went virtually unnoticed during the 1970s and 1980s, over the past twenty-five years it has become a worldwide matter of high priority. Indeed, it is clear that since the 90s, the interest in inequality and its impact on economic efficiency has increased significantly, especially among scholars (Sen, 1995; Stiglitz, 2012; Piketty, 2014; Krugman, 2014) and politicians (Lula da Silva 2006; Obama, 2014, Bachelet, 2014).

Starting in the 1990s, associated with the neoliberal wing inside neoclassical analysis, a specific vision began to gain primacy. Inspired by this approach, a large number of studies declared that there was no evident relationship between growth and inequality and it would be reasonable to conclude that, in general, *"growth is good for the poor"* (Dollar and Kraay 2001), whatever its nature (Deininger and Squire, 1997; Li and Zou, 1998; Li, Xie et al. (2000); Ali and Elbadawi, 2001). Adopting this line of analysis, several authors tried to establish the presence of an innocuous relationship between growth and inequality. Ravallion and Chen (1997) and other authors such as Foster and Székely (2001), suggested that growth would reduce inequality.[197]

Other empirical studies (Li and Zou, op. cit.) which compared the economic performance of a large number of countries since 1960, examining whether higher levels of inequality at the beginning of that period were associated with the worst or the best

197 In the case of these last authors, the evidence of their study was clearly insufficient and their hypothesis would not be proved if countries in Europe and Eastern and Central Asia were removed from the sample.

subsequent economic performance, reported finding a positive relationship between income inequality and growth.[198]

The "discovery" of a positive relationship between inequality and growth seemed to revive traditional economic thought (Kuznets, 1964) which postulated that, by concentrating income amongst a small group of wealthy individuals was positive. Firstly, greater inequality would increase the saving rate of the economy and secondly inequality would install incentives to work harder and move up the social ladder.

Following these two pathways, neoliberal argues that inequality would be a mere problem of speed adjustment of the economy, but would eventually favour economic growth. However, in our opinion, the relationships documented by some Chilean studies linked to such approach, defending the positive role of inequality, an idea passionately defended by Chilean neoliberal authors (e.g. Kaiser, 2015), are not solid.[199]

On the other hand, some non-neoliberal arguments have highlighted that, ceteris paribus a certain rate of growth of GDP, the trajectory of the reduction of poverty tends to be faster when inequality is smaller. According to this argument, as poverty is associated with lower investment in human capital and lack of access to credit due to lack of collateral (situations that growth requires be overcome), maintaining this would generate a trap in which inequality associated with poverty would erode the growth rate. As is it possible to see, the differences between both formulations are quite acute.

In the period under analysis, these academic discussions have also been held in Chile, but accompanied by a strong political emphasis. In Chile, when right-wing parties and neoliberal scholars defend the existence of a positive relationship between inequality and growth, they are defending a set of institutions and arrangements which, in the

198 In general, some of these models used data panels that took into consideration certain problems of endogeneity of the laggard dependent variable, but they also obtained a positive relationship between income inequality and economic growth.

199 From a global perspective, another problem identified in international studies as a cause of the difficulty of accurately identifying the relationship between inequality and growth, refers to the fact that the data on inequality whose quality is not uniform often presents problems. Sometimes it is not clear that the indices obtained are comparable internationally. This is because the methodologies used to calculate indicators of inequality in different countries might differ significantly, so it is possible that the empirical measurements that researchers used contain large errors.

Chilean case, led to a sustained economic growth that accentuated social inequalities but, they believe, would drive the Chilean economy towards development.

From that perspective, they consider that followed the most appropriate path for growth, considering their own proposals as a rigorous base to build "serious" distributional policies. At the same time, they evaluate distributional policies of post dictatorship governments as "premature"; describing them as a brake on the process of economic development that followed trade openness and which they appraised as extremely positive, minimising problems linked to income disparity (Sanchez y Soto, 2015).

Paradoxically, during the studied period, post dictatorship governments has become to share this approach, considering which, impulse of distribution process during their administration would not be a sound policy, being better only implement social policies based on subsidies and cash transferences programmes (CTP) supported in bigger taxes that has not a progressive character (like value added taxed, the main source of public resources existing in Chile).

While the Chilean centre-left parties were opponents of the dictatorship, they strongly criticised the trickle-down model as being useless to alleviate inequality. However, when they arrived in government after 1990, they did not try to implement substantial changes in the former development model. They chose rather not to abandon the fundamentals of the neoliberal model and not modify their economic institutions, with the aim of "protect economic growth" and "discourage implementation of statist policies" (Boeninger, 1997).

In order to analyse this complex issue, we will try to illustrate discussions relevant to the analysis and perspectives of the Chilean economy, showing how even when Chilean trade openness has been associated with higher rates of growth, it has maintained a stagnant distribution of income affecting the overall efficiency of the economy.

6.4. Institutions and Income Distribution

Since the start-up period of the neoliberal model, as in the course of its consolidation in the post dictatorship period, the Chilean economic mainstream has been dominated by the idea that the reduction of poverty exhibited by the economy can be explained by the high average growth rates which it exhibits (Larrañaga 2001; Hench, Broncos et al, 2010).

From this point of view, it has been argued that growth has been good for the poor and the persistence of significant levels of inequality have not affected the continuous decrease of poverty. The neoliberal approach assumed that poverty would be a variable that would decline in the near future, step by step, without generating negative externalities to the economy.

They assumed that a tax reform or state interventions in the economy oriented to poverty reduction would be intrinsically distortive, producing negative externalities and halting automatic evolution of the economic development. Thus, they considered that the elimination of poverty would not require institutional changes which looking for a lower inequality, but would only necessitate the maintenance of the neoliberal reforms already implemented during the dictatorial period (Harberger, 2015).

In short, the neoliberal perspective is dominated by scepticism about the possibility of achieving medium-term lower inequality of incomes by state actions over institutions, without produce a deterioration in rates of economic growth. (Katz, 1984; Beyer, 2011; Fontaine, 2012; Larraín, 2012). In addition, assessment from non-neoliberal's economists (Foxley 1993; Collins and Lear, 1995; Diaz and Martinez 1995; Arellano 2012), in several points agrees with the above point of view.

Even they do not advocate for a greater disregard of the State in social policy, their evaluation is that Chile has made significant achievements, not only economically but also socially, given the positive impact of (neoliberals) policies applied to date.

During 1990-2009, new Chilean authorities declared that their policies would be focused on low-income groups, drastically reducing the negative social legacy of the military dictatorship at the poverty area. However, this problem did not accept simple solutions. As corollary of the neoliberal model implementation, Chilean economy had produced a paradoxical situation in which not only is it possible to observe a sustained and relevant fall in headcount poverty, but parallel, a consolidation of important inequality levels in the Chilean economy.

The improvements in the poverty area has not obeyed an economic policy that improves the competition dynamics of the markets and change the neo-liberal arrangements aimed only at the generation of economic rents.

During the dictatorship period, the Chilean State has reduced poverty through a combination of expansion of precarious employment and the implementation of focalized social policies based on subsidies and monetary transferences.

This approach to the reduction of poverty had been caustically criticized by leading economists opposing the dictatorship, however once they took, later in 1990, driving economic and social policy, its new policy differed in very little of the neo-liberals. Its emphasis was put on increasing the coverage of the old programs and in the creation of some new covering new social areas still without coverage, but the old neo-liberal approach to social policies was maintained.

However, poverty not only reduces depending on social policies, but that economic market´s efficiency plays a role of great importance and the growth process depend, in a very close way, to evolution of economic efficiency. It has been estimated that in the medium to long term, the Chilean economic growth will bring about a reduction in the poverty of a magnitude similar or superior to the rate of growth of GDP. If you notice the evolution of poverty represented in Figure 6.1 that statement seems quite reasonable, however it is necessary to analyse in greater depth the evolution of poverty in Chile and effectiveness of the devices used to achieve its significant reduction, before develop definitive conclusions.

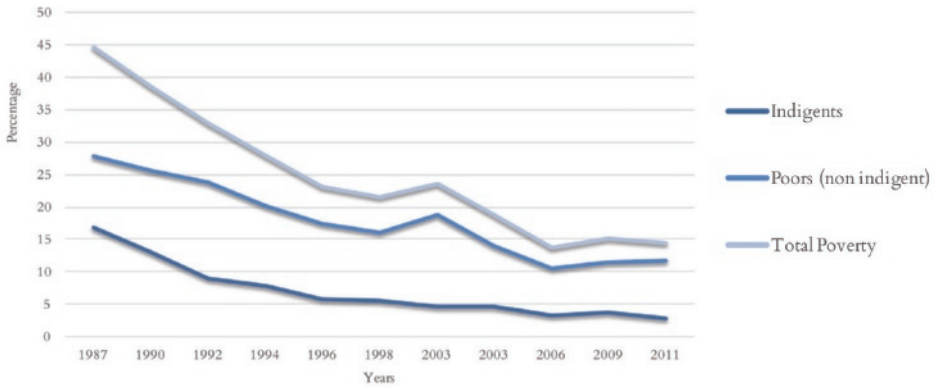

Figure 6.1. Poverty Reduction. Chile: 1990-2009.
Source: Author´s elaboration based on data of |Chilean Ministry of Social Development. CASEN Surveys: 1990-2009

6.5. The Different Varieties of Poverty

The variations in the levels of poverty in a country can be estimated in different ways; the most widely used are the Foster-Greer-Thorbecke (FGT) indexes (Foster, Greer and Thorbecke; 1984, 2010). Within that framework, we will name **P** as any of the poverty measures proposed by these authors. The empirical general calculation of FGT is as follows:

$$P\alpha = 1/n \sum_{n=1}^{q} ((z\text{-}yi)/z)\alpha$$

In that indexes, usually:

Y: Is per capita GDP, income, or expenditure e.
z: Is the poverty line,
y_{es} : Is the i-th lowest income (or other standard of living indicator),
y_{av} : Is the average income of poor,
n: Is the total population,
q: Is the number of persons who are poor, and
α: (alpha) is a "poverty aversion" parameter that is a real non-negative number with three possible values: 0, 1 or 2.

There are three possible estimations of GFT indexes. Since P is an average over the total population, n, the distances that separate individuals or households on the poverty line; an exponent α weights this average.

The value of the exponent allows that the same formula can be used in any of those three cases: When α = 0 we will have the GFT- P_0 index which will reflect the "Incidence of Poverty" (or headcount index), which is the percentage of individuals whose income is below the poverty line. Then P_0 will decrease their value upon the occurrence of a decrease in the percentage of poor individuals. The form of this first index is:

$$P_0 = \frac{q}{n}$$

When α = 1, the GFT- P_1 index will reflect the "Average Poverty Gap". This gap reflects the average shortage in resources within the poor population that is estimated

as the incidence of poverty multiplied by the absolute gap of income, a gap that is equivalent to the distance among average monthly incomes of poor or extremely poor populations and their respective poverty or indigence line. Then P_1 will decrease upon the occurrence of a decrease in the gap. The form of this second index is:

$$P_1 = \frac{q}{n}\left[\frac{(z - y_{av})}{z}\right]$$

Finally, if $\alpha = 2$, GFT- P_2 index will reflect "Depth of Poverty" which incorporates a measure of income distribution within the group of poor households or individuals, marking differences within this group. The Poverty Depth index is measured as a weighted average of the squared distance below the poverty line, expressed as a percentage of that line. The weights are usually given by each individual gap. Since the weights increase with poverty, this measure is sensitive to inequalities among the poor. That is why P_2 is the summation of the differences between average incomes of poor persons (or households) and the poverty line value, weighted by participation of the poor in total population. The form of this third index is:

$$P2 = \frac{p}{q}\sum_{k=0}^{n}\left\{\frac{z\text{-}yav}{z}\right\}$$

An estimation of these three indices and its evolution between 1990 and 2009 is shown in Figure 6.2: (A and B). In that Figure we can see, in superior line (red line), Incidence of Poverty (i.e. the percentage of poor people within the total population. In intermediate line (green line), we can see the Average Poverty Gap (i.e. the difference in absolute values of poor income in relation to the poverty line, multiplied by the incidence of poverty). This Gap also represent the amount of monetary resources needed by the poor (as a proportion of the poverty line) to surpass their condition.

In the inferior line (blue line), the Depth of Poverty (i.e. the square difference in absolute values of poor´s income in relation to the poverty line, multiplied by the reciprocal of total population) is displayed. From 1990 to 1994, those indexes drastically reduce their values, from 1994 to 2006 reduction become slower and after 2006, the indexes reverse the former tendency. Evolution of known GFT-P_0 index (poverty incidence or, the percentage of poor within the Chilean population) graphed in Figures 6.2A (blue line) shows an impressive reduction in the relative and absolute numbers of poor population. Contrariwise, the situation is not the same if we analyse the poverty

reduction performance using indexes based on the "poverty gap" (green line) or "depth (severity) of poverty" (red line).

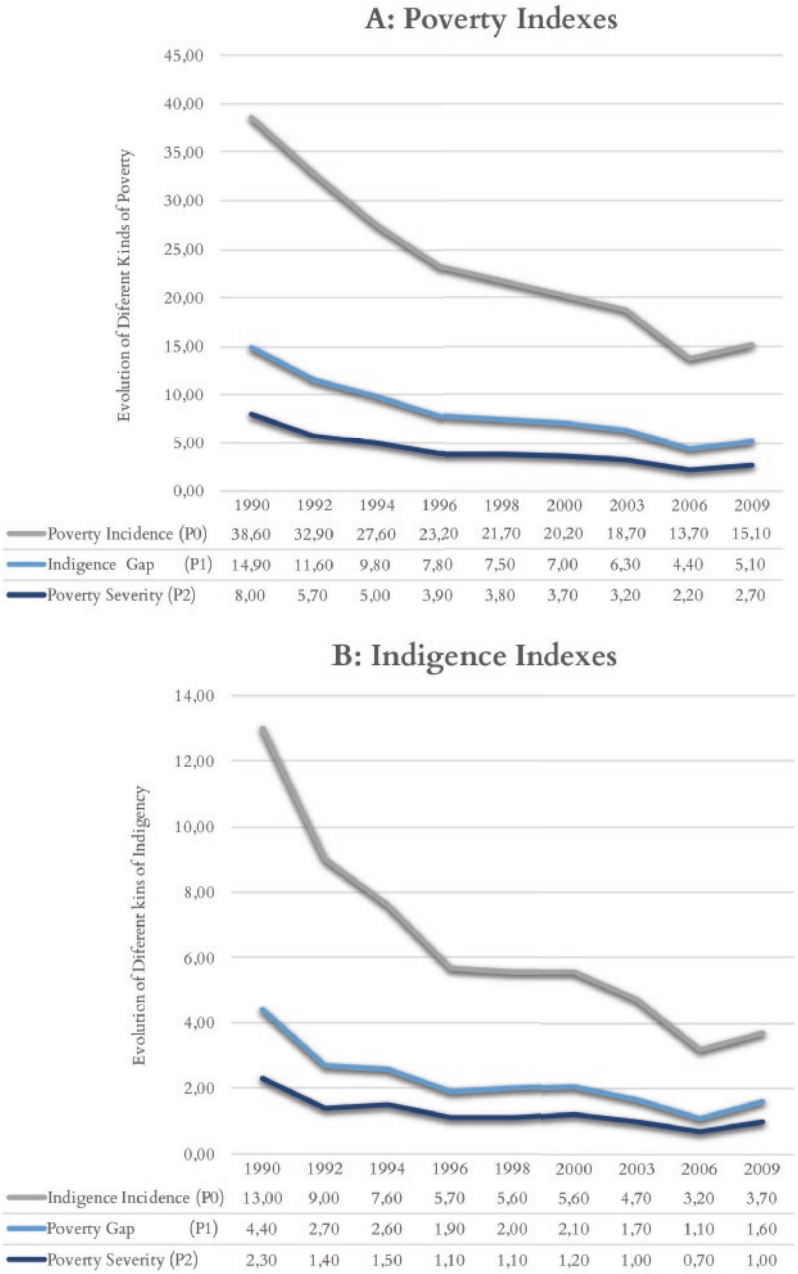

Figure 6.2. Depth, Incidence and Poverty-Indigence Gap. Chile: 1990-2009.
Source: Author´s Elaboration using Casen Survey1990-2009 Micro data. "Poverty condition" includes Poor but non-indigent population, plus Indigent population.

During the analysed period, GFT-P_1 index (Average Poverty-Indigence Gap) has also decreased but at lower rates than P_0 index (Incidence of Poverty-Indigence). There is no doubt a reduction in distance of the average incomes of the poor with respect to the monetary value of the Poverty-Indigence line. However, the rate of such reduction has been diminishing over time, in parallel with the growth of GDP per capita.

With regard to the GFT-P_2 index (Poverty-Indigence Depth) which includes income distribution among individuals or groups of poor-indigents individuals (red line), we can observe that income inequality within the poor has been also decreasing, but at a smaller percentage than poverty-indigence incidence. That means that, throughout the period 1990-2009, the distance that separates average incomes of each group of poor from the poverty-indigence line, weighted by their share on total population, has been decreasing, but in a less significant way each year.

Beyond the original forecast of Chilean neoliberals and their economic development model, the outcome was a "pro-poor growth", strictly framed within the definition proposed by Ravallion and Chen (2003) and by Kraay (2004): "The growth is pro-poor if the poverty measure of interest (not only headcount index) falls". Despite the positive pro-poor trend of those three indexes during the period 1990-2006, towards the end of the analysed period, i.e. 2006-2009, we can observe that all of them showed a serious setback. The same thing happens in the case of indigence, whose tendency to reduction is less dramatic and exhibits more ups and downs in the case of poverty incidence. In addition, the GFT-P_1 and GFT-P_2 indices show a decreasing capacity of the economy to reduce those types of poverty. After the first big reduction identified between 1990 and 1996, indigence remains almost constant until 2000, falling again until 2006, but rising since then until 2009.

In figures 6.2A and 6.2 B we can also see that regardless of which method of measurement poverty-indigence that we are using,[200] the three variables determining poverty-indigence (Incidence, Gap, and Depth) are not affected in the same way. All kinds of poverty-indigence are falling, but not to the same extent. That situation suggests that defining the presence of the positive tendency of explicative variables is not enough to

200 The three measurements analysed here are all carried out from a "relative monetary poverty" estimations. One of the essential questions in that interpretation of the phenomenon of poverty is the degree of mobility of individuals between different strata of monetary incomes. The estimation of rates of multi-dimensional poverty go beyond the scope of this research and, additionally, data does not exist allowing such estimates of that kind of poverty during our study period.

understand the performance of poverty-indigence in relation to the growth process. The determinants of all these trends are closely linked to the evolution of the absolute gap of poverty or indigence. Both tendencies are more clearly expressed in Figure 6.3.

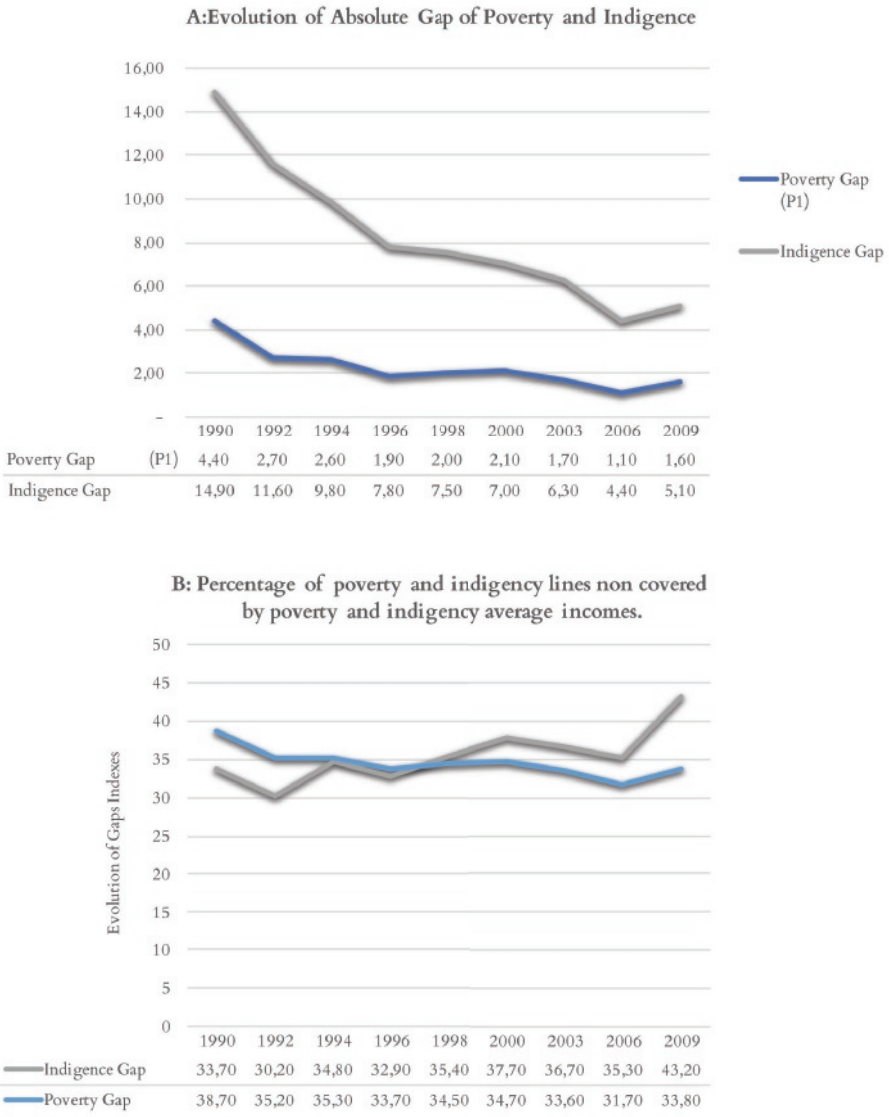

Figure 6.3. Poverty-Indigence Gap. Chile: 1990-2009.
Source: Author´s elaboration using Mideplan-Casen 1990-2009 Micro data.

There we firstly can see (in Figure 6.3A) that from 1990 to 1998, the absolute gap (red line) between average income of the indigents and the indigence lines decreased systematically.

In the case of indigence, during 1990-1998 the gap fall from 4,4% to 2,0%, to 1,1% during 2000-2006, increasing to 1,8% in 2009. In the case of poverty, during 1990-1998 the gap fall from 4,9% to 7,5%. In the case of poverty, the gap fall, during 1990-1998, from 14.9% to 7.5%, the gap fall from 7,0% to 4,4% during 2000-2006 and increase to 5.1% in 2009.

The reductions in poverty and indigence gap are not a minor achievement, because they involve a significant reduction of the amount of money (estimated as percentage of poverty-indigence line), that is necessary to let people jump those income barriers. In fact, the poverty gap drops in 20 years to a level very close to 65% of the original, and close to 64% in the case of indigence gap

In Figure 6.3B we can see that from 1990 to 1996, the ratio concerning the absolute gap between average income of the poor and the poverty line, weighted by headcount index (blackline), is fast decreasing. From 1996 to 2003, that tendency slows, but from 2006 to 2009 both gaps increase again. However, if the indigence gap (red line) is analysed, the state of affairs worsens dramatically because that gap decreases significantly only from 1990 to 1992 (from 4.4% to 2.7%).

After those years, the gap decreases slowly so that in 2006, the average income of the extremely poor population was only 1.1% below the indigence line. However, in 2009 the gap increased again to 1.6% in such a way that the government goal of achieving a level of indigence less than 1% in 2014 was not reached. That was a goal that gave the impression of being easy to obtain in 2006, but a few years later (2009) it was clear that this aim was much further than expected and even in 2016, a decade later, this target continues to be seen as extremely difficult to achieve. That situation shows that the proportion of people below the indigence lines is still diminishing, but the distance between the average income of people that remain as indigent and the indigence lines is increasing, making it more difficult each year to reduce the number of extremely poor people.

Both lines (red line and black line) shown in Figure 6.3B give a clear idea as to the fragility of the process of poverty-indigence reduction and about the elements that, within the Chilean growth process, exert influence over poverty-indigence reduction. These figures also show us that, in the Chilean case, the behaviour of the relationship between economic growth-poverty (indigence) is far from being a bi-univocal relation, independent of poverty-indigence variety that we decide consider

as pertinent. Nevertheless, to define characteristics of the relationship existent among such variables requires estimations that are more accurate.

6.6. Growth Influence on Poverty Reduction and Income Distribution

Given that Chile´s GDP growth evolution has exhibited different changes over time, we can expect in some periods a worsening of the process of poverty reduction and income distribution, and an improvement in other periods. From that situation, we can assume that GDP growth may produce changes in the dispersion of incomes of people and families, and starting from that circumstance, changes in the share of the Chilean population living under the poverty line. For that reason, despite the fact that in some years of the analysed period, changes in the number of people under the poverty line look to be a consequence of growth acting in a unidirectional form, without affect inequality, but the causal relationship among these variables give the impression to be more complex.

Income distribution may affect poverty evolution in at least three interrelated dimensions. The first one is the average income growth, the second is the income dispersion and the third is the proportion of people below a certain income level (e.g. poverty line). In general, it is sound to assume that the three effects are interrelated and both the initial value of each one and its variation will have consequences on the final distribution of income. Bourguignon (2004:2) asses that changes in poverty are related to the growth in average incomes which, produce changes in the dispersion of income and reduction of absolute poverty levels. He identifies this relationship as the "Triangle of poverty, growth and inequality" (op. cit.), a concept that we will use to analyse the problem that concerns us.

Changes in the growth of income as changes in income inequality play an important role in determining the level of poverty changes brought on by income distribution. Both changes can be separated into two effects:

- Firstly, there is the effect of a proportional change in earnings, which leaves intact the dispersion (or "growth effect").
- Secondly, there is a change in the dispersion of income that does not affect its grade point average ("distributional effect).

Figure 6.4 suggests that the distributional effect has lacked major impact compared to economic growth. In this figure, the Gini coefficient, which measures the distributional changes, has remained almost unchanged after moving erratically, whilst GDP growth has been robust and the reduction of absolute poverty significant.[201]

Based on the performance graphed in Figure 6.4.: Is it possible to accept the neoliberal argument sustaining that growth was the only tool that would make it possible to overcome poverty, therefore all kind of economic growth would be good for the poor? We believe that this assessment is not supported on available information.

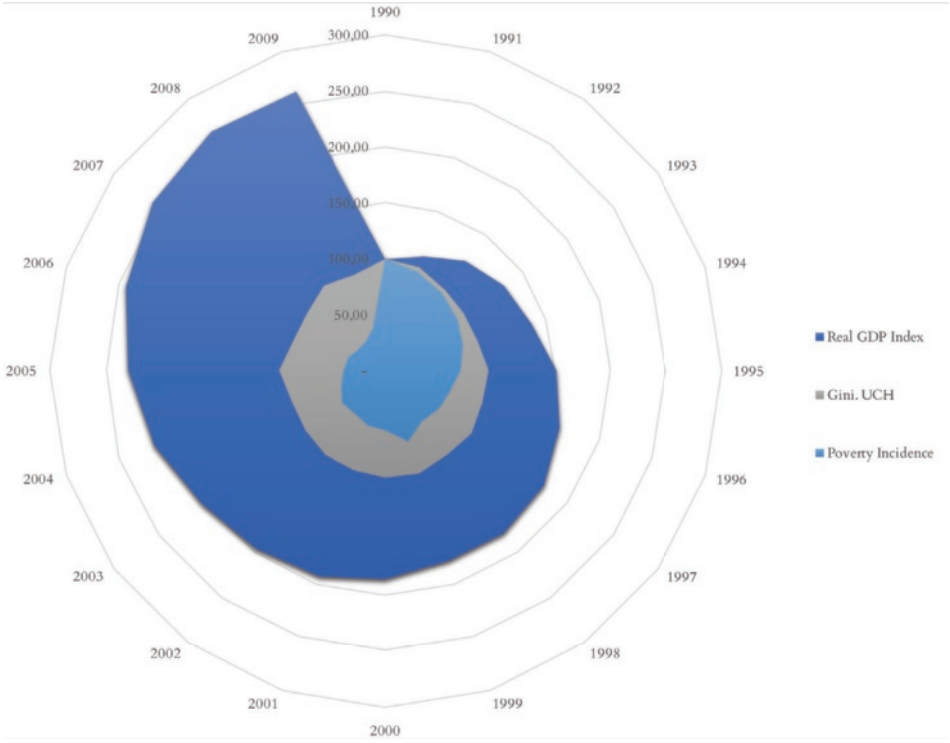

Figure 6.4. Evolution of Poverty, Income Distribution and GDP Growth. Chile 1990-2009. Source: Author´s elaboration based on: GDP, Central Bank of Chile in CL$ 2003; GINI, University of Chile; Poverty; CASEN 1990-2009. Indexes 1990 = 100.

201 Similar conclusions have also been extracted in the studies on the subject of Contreras (1999) and Larrañaga y Rodríguez (2014) who find that in Chile output growth trajectory is not correlated to significant decreases on inequality and only some years is correlated to decrease on poverty

As poverty reduction was not an instantaneous phenomenon, they assume that the progression of the opening and liberalisation of markets and the presence of certain social segments which were not covered by the evolution of the economy (single mothers, elder people, kids in situation of social risk, handicapped, etc.) required a policy of direct subsidies. However, in their view, these transferences must be targeted only in these sectors. In other words, for neoliberal view, the redistributive component of public policies should have, as a central point, the offset of frictional costs of market´s. liberalization. Thus, it is not surprising the low impact of income redistributive policies that have followed this orientation, e.g. the Chicago boys and the post dictatorship Governments´ policies.

In addition, and based on the same approach, neoliberal economists declare which, for that reason, the new policies, who sought to expand the scope of these instruments, ultimately would operate against the effort of poverty reduction. The new generation of economists that arrived at the Chilean Government in 1990 tried to oppose this analysis with the idea that isolated growth would fail to maximize outcomes of their poverty reduction actions, at least if the new governments does not apply some progressive social policies that would pull out growth effects.

Despite this, the successive governments post dictatorship, did not associate their policies to introduction of public´s actions oriented to produce changes in the primary distribution of income. On the contrary, their focus was placed only on the impact that their new social policy could exert both on the reduction of poverty and on income distribution, understand the last one only as a by-product of their social policies. Authors like Cowan & De Gregorio (1996) and Meller (2000), economists of great influence within the new governments, analysing the impact of social policies implemented by the first post dictatorship government, argue that social policies have a strong impact on other factors. They emphasize influence of public expenditure on education and health, which would have tended, in their opinion, to offset the increasingly unequal distribution of income.[202]

202 The measurements of both Meller as Cowan-De Gregorio have a common problem. They do not adequately differentiate the concepts of elasticity and semi-elasticity. Both papers calculate elasticity growth of poverty using in the numerator, percentage points of variation of poverty and in the denominator, percentages of variation of the GDP, which allow them to declare that they are estimating the growth elasticity of poverty, when in reality they are estimating the growth semi-elasticity. Then the "efficiency indicator of growth in reducing poverty" used in both studies, ends up being an estimate of elasticity obtained from normalisation of semi-elasticity (and not of elasticity), because it multiplies in the denominator, the percentage variation of the GDP by the initial value of the poverty. This is a situation

Following their arguments, it would be wrong to split the income growth of the poor from the impact of aggregate growth of the economy and from the distributive impact of social policy, neglecting the mutual interactions existing between growth and distribution. They argue that firstly it is necessary to identify the increase in the income of the poor that should be attributed to social policy and, after that, identify the impact of the rest of the factors on that income growth. However, in a paradoxical way, the point of view of these (and others) non-neoliberal economists changed with the passage of time, assimilate to the neoliberal vision about evaluation of policies for poverty reduction, without establish serious differences with that point of view.

For example, Larrañaga y Sanhueza (1994), applying the methodology of Gottschalk and Danzinger (1985) in a sample of the Chilean population disaggregated into 15 groups of economic activity and level of education, concluded that 90% of the headcount poverty reduction in Chile is explained by economic growth.

In the same vein, after analysing growth elasticity of poverty and the effectiveness of social policies, Contreras (1996) concluded that in Chile, during the period 1987-1992, 73% to 83% of poverty reduction should be linked to economic growth. Subsequently, using the methodological proposal of Ratt and Ravallion (1992) to analyse the period 1987-1994, Contreras and Larrañaga (1998) and Contreras (2000), essentially confirm their previous conclusions. Nevertheless, they attribute to economic growth only 80% of the achieved poverty reduction, adding that the remaining 20% would be explained both by the distribution effect, as well by a residue of smaller relevance.

Other authors like Urmeneta (1996) and the World Bank (1997), after analysing the 1987-1994 period from a somewhat more nuanced perspective, also conclude that the reduction of poverty in Chile has been highly correlated with economic growth. They stress that, when this growth declined among 1992-1994, the reduction of poverty also slowed and social policy improved the standard of living of the people that avoided worsening poverty. They argue that it would be through the generation of autonomous incomes in the labour market that the bulk of the reduction in poverty has been produced. Last of all, the research of Meller (2000) went a step beyond those conclusions and based on the estimation of growth elasticity of poverty, estimated that during the period 1990-1996, economic growth would explain only 60% of the

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that makes the conclusions drawn by the authors quite confusing, even more so when we remember that the data used in these studies was provisional and has been subsequently corrected, both by Mideplan as by the Central Bank.

reduction of poverty, while the remaining 40% would be an effect of social policies implemented since 1990.

Even before analysing whether trade-openness and market-liberalisation really are the variables which produced the high rates of GDP growth shown by Chilean economy, based in afore mentioned studies and in a plenty of other research's, it is clear that growth rates contributed in a very important way to poverty reduction. However, neoliberal forecasts about that GDP growth would produce an improvement of people´s incomes, given by the increment on their autonomous incomes because of wage alignment with improved labour productivity, constitute an assessment that is not supported in empirical evidence.

The neoliberal economic theory sustains that as long as less productive workers are reassigned from sectors of low productivity to high productivity, wages should increase proportionally to the productivity improvement of that kind of labour, acting in a new and more productive framework. However, given that these processes are not instantaneous, they sustain it would require longer efforts over time to protect those people who remain marginalised from the labour market (elderly, children, single mothers, workers in sectors of difficult re-conversion, etc.). The means by which they should be protected throughout implementation of "targeted social policies". Those policies, it is said, would make the process of reallocation of resources more fluid, whilst the new dynamic introduced by trade openness and liberalised markets would reduce frictional problems to a minimum, allowing some degree of decompression of the social and political conflicts that typically accompany the processes of liberalisation.

Contrary to what is asserted in that assessment, we will demonstrate in the course of this chapter that economic growth has not played the role that neoliberal proposal attributed to it in terms of the reduction of poverty. Additionally, we will demonstrate that the social policies have not played the decisive redistributive role forecasted by centre-left wing governments during the nineties.

As we have previously seen, income distribution is related to the interface between GDP growth and the evolution of autonomous incomes, determined in turn by the dynamics of the labour markets. Accordingly, the low decrease in inequality observed in Chile over the analysed period, is a situation that, in our opinion, could be attributed

to a combination of some minor gains in terms of employment, and a diminution of autonomous income´s share for the bottom quintile of the income distribution.[203]

Analysing the Chilean case, Marcel and Solimano (1994) found that one of the main factors that explain the drop in the share of the poorest quintiles on the national income is the increase in the unemployment rate. Accordingly, it would be reasonable to assume that an important amount on the changes of incomes of the poorest, observed between 1992 and 1994, are explained by changes in the labour market. On turn, we considerate that this dynamic was highly determinate, firstly by settled institutional arrangements and secondly by the formerly described (Chapter III) institutional environment.

Like has been displayed at Figure 6.6, diminution of autonomous income´s share of poorest quintile, drops from 4.1% in 1990 to 3.6% in 2009, but it was compensated by the positive influence of a wide battery of targeted public transferences that allowed that monetary income in the lowest deciles to increase from 4.3% in 1990 to 4.6% in 2009. In fact, as we will analyse in this chapter, despite the wide battery of social programs that were applied, the regressive trends in the autonomous income distribution ensured that poverty reduction lost its dynamism, moving slowly initially and later in a contrary sense of GDP growth.

For the purpose of analysing more carefully this phenomenon, we have proceeded to estimate at least two indicators of the relationship between poverty and economic growth:

- The Growth Elasticity of Poverty
- The Growth Semi-Elasticity of Poverty

6.7. The Growth Elasticity and Semi-Elasticity of Poverty

The traditional way to estimate the kind of interrelationships existing between poverty and growth is to analyse the behaviour of the "Growth Elasticity of Poverty" (e) a

203 According to the 2009 CASEN survey, that year 31.5% of poor people were unemployed. Whilst only 7.9% of people classified as "non-poor" were unemployed. Moreover, in 2009, the average income of the 2 first income deciles were only 18% of the average income of third and quarter deciles, and 6.4% of the average income of the ninth and tenth deciles (CASEN, 2009)

variable that formally shows the extent to which growth has translated into poverty reduction,[204] assuming as ceteris paribus the initial level of inequality and the degree of poverty. It can be expressed as:

$$\mathcal{E}\mathcal{E}=\left(\frac{dP}{dY}\right)\frac{Y}{P}\left(\frac{dP}{dY}\right)\frac{Y}{P}$$

Where P is any of the Foster-Greer-Thorbecke (FGT) poverty measures and Y is per capita GDP, income, or expenditure per capita.
There are multiple ways to measure this elasticity (Deaton, 2013; Atkinson 2015) which assume that the logarithm of income per capita (or household consumption), could behave -under certain conditions- in the same way as a lognormal distribution. The expected result is the presence of an inverse relationship between GDP growth and poverty reduction; in our case the elasticity measurement, period-to-period (arc-elasticity), will not only show whether this negative trend exists in a permanent way, but it will also show us the existing proportion between magnitudes of changes in both variables associated with that trend.

In our case, the Growth Elasticity of Poverty was considered as a measure of the poverty-efficiency of growth and was estimated as the ratio of the annual relative (percentage) change in poverty rate with respect to the relative change in the annual change in real GDP per capita during each period (Bourguignon, 2003). This ratio measures how a one percent increases in the rate of growth affects the FGT poverty measures|. That method has been formerly used in the Chilean case by several authors (De Gregorio 1993; Meller 2005; ECLAC, 2008). Nevertheless, growth elasticity is widely used a measure of the efficiency of the economic growth to reduce poverty, authors as Klasen and Misselhorn (2006), suggest as an alternative to use Semi-Growth Elasticity as a different measure of the sensitivity of poverty reduction to economic growth, estimating it as the percentage change in terms of percentage point changes in poverty reduction.

204 The total growth elasticity of poverty reflects many different changes, such as variations in inequality, initial level of inequality, initial level of development, growth rate, and data issues. For this reason, that indicator should be interpreted carefully. For instance, if we compare two economies, ceteris paribus the same level of poverty, the economy with a high growth rate and lower growth elasticity will not necessarily be pro-poor in relation to the other one (World Bank, 2005:81).

Designers of that ratio point out that using percentage changes in poverty reduction (as growth elasticity of poverty do), findings may be easily misinterpreted. For instance, if the initial poverty headcount (or any other FGT index) is relatively low, then a small absolute reduction in poverty can constitute a large percentage change in poverty.[205]

In order to avoid misleading interpretations associated with that kind of limitation of elasticity measurements, we decided to compare the measurement of both parameters (elasticity and semi-elasticity) in order to analyse in greater depth, the real impact of growth evolution on poverty in the Chilean case from 1990 to 2009. Given that, in this study, the arch-elasticities of each one of those periods were estimated from discrete data, firstly, we estimated the growth elasticity of poverty; secondly, we estimated the Growth semi elasticity of poverty.

In figure 6.5, we can see that the growth elasticity of poverty shows a general trend quite similar to reported on the literature in countries like Chile. However, the general trend shows two severe inflections, both external to the Chilean economy (e.g. the shocks associated to the Asian Crisis of 1996-1998 and the crisis sub-prime from 2007-2009). Between 1990 and 1997 the elasticity of the three types of poverty analysed here had been negative and stable, despite the slight retreat of the distribution of monetary income occurring between 1992 and 1994 due largely to changes in the labour market. These were caused by cyclical variations in economic activity and, therefore, did not become a structural trend until the beginning of 2008, when Chile began to feel the effects of the sub-prime crisis. From that year, the elasticity becomes positive; however, since 2009, this situation is reversed when the effects of this external shock on the Chilean economy disappear.[206]

205 Let us suppose two countries, the first one with 50% of poverty incidence and the second one with 5% of poverty incidence. If GDP per capita increases by 10% yearly in both countries, as a consequence of that, in both countries, we will have a 50% of poverty reduction; in the first one, poverty would have reduced 25 percentage points and in the second one only 2.5 percentage points, but in both countries growth elasticity of poverty would be equal to - 5. Then, the assessment that a rate of one per cent of economic growth will produce a poverty reduction of five per cent would be distorting our view of poverty problems if we assume that in both cases the situation was the same.

206 The elasticity of observable positive sign from the crisis sub-prime pollutes the general trend for the whole period. If the period 2008 2009 out removed from the data, the elasticity of the period 1990-2006 would be negative and growing, with average values close to two in absolute values.

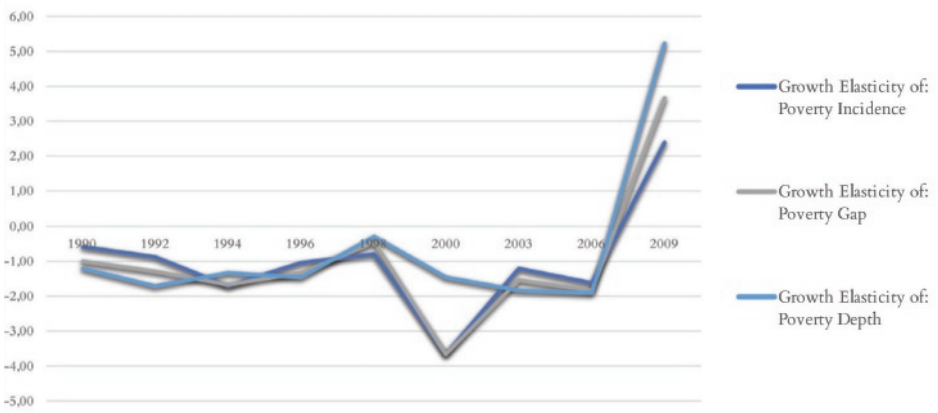

Figure 6.5. Evolution of Growth Elasticity of Poverty
Source: Author´s estimations using Micro data of Mideplan-Casen surveys 1987-2009, INE population census and Chilean Central Bank.

Except for the identified breaking points, the evolutionary trend of the three FGT indexes shows a sustained decrease in the absolute values of the respective growth elasticity of poverty. All growth elasticity's have the same evolutionary path. However, the comparative analysis of the different measurements of poverty shows evolutionary trends of different magnitude in each particular case. But all values suggest that economic growth has been positively related to poverty reduction. In our estimates of the growth elasticity of headcount poverty over the period 1990-2009, Chile presents an average elasticity of (-1.4), but if triennium 2006-2009 is excluded, the average growth elasticity is equal to (-2). That range is very consistent with worldwide available evidence for developing countries, but does not explain in a clear way why there was not a faster reduction of poverty in a period in which GDP per capita increased in real terms by around 98%, but poverty was only reduced an 67%.

If we analyse the average tendencies closely it is possible to observe which varieties of poverty display a unique tendency throughout almost the entire period, but with a severe divergence during the sub-period 1998-2000, which reflected the impact of the Asian crisis, headcount and gap elasticity's increase their absolute values, yet there is a reduction in the GDP growth rates. However, that does not mean the reinforcement of a pro-poor path of development, reflected in high elasticity's. For instance, the high estimates of headcount poverty elasticity must be interpreted with reference to the fact that we are not evaluating how much poverty has been reduced in a period of fast economic grow. Instead, we are evaluating headcount poverty reduction from

23% in 1996 to 20% in 2000, associating it with a period of collapse in GDP growth (from 15% in 1996 to 0.95 in 2000).

During that external shock, Chile's GDP per capita growth remained positive. However, the absolute values of those three poverty-elasticity's, even with a negative sign, showed a different behaviour. In fact, at the height of the crisis (1998), a fall of 1% in GDP would produce a reduction of 0.91%, 0.54% and 0.36% in headcount, gap and depth of poverty respectively. Growth elasticity of the depth of poverty presents the worse behaviour. It fell to a very low level in comparison to the previous two poverty varieties. Nevertheless, as in our exercise, the three types of poverty measurement are carried out using monetary incomes, is clear that social policies played some role in the achievement of those results.

The Chilean authorities post dictatorship evaluated the general path followed by the economy during the nineties as being a pro-poor one. In order to then avoid a reduction in the effectiveness of their poverty reduction strategy, they widely used different instruments of social policy, trying to limit the crisis´ effects on the low-income segments in which social spending was focused. Since 2000 onwards, Chile began to recover from the effects of the Asian crisis, growing 6.17% between that year and 2003, and by 13.42% between 2003 and 2006, hence the return of growth elasticity to its normal values along the 2% annual.

From that year onwards, those three elasticity's show signs of change and we can observe a very similar increase in the variation rates of the three types of poverty associated with GDP PC growth rates. If the behaviour of the Chilean economy in this respect is viewed within the parameters of international experience, we must remember that the literature assesses that growth is significantly beneficial to the poor when the elasticity of poverty with respect to GDP exceeds two points.[207]

If it is between one and two points, it benefits them moderately; whilst they are harmed when it is less than one point (Cling et al, 2004). In the Chilean case, our estimates show that between 1990 and 2009, the average growth elasticity was far below the levels required to contribute seriously to the sustainable reduction of poverty. In any case, in general it can be concluded that in terms of gains to the poorest population, Chilean economic growth can be defined as of moderate to low impact.

207 Bourguignon, (2003) reports that worldwide those elasticities are usually located around 2%.

In summary, the general trend of the moderate impact of growth on poverty is reflected during the analysed period by means of a decrease in the three-growth elasticity of poverty varieties, a tendency highly conditioned by the presence of elevated levels of economic growth. When GDP growth declined, poverty reduction began to slow, and it slowed even more when low growth rates (close to 2% between 2006 and 2009) were installed, causing growth elasticity to be positive during the last triennium. The presence of this growth elasticity behaviour shows how precarious the process of poverty reduction recorded in the Chilean economy is. Gradual trends as to the minimisation of the impact of growth on poverty were slow at first, and then affected by external shock, those tendencies meant that the sign of growth elasticity of poverty become positive.

All this is conclusive proof of the weakness of the influence of the growth process of Chilean economy on poverty reduction. If, in the long run, development policies intend to reduce poverty without intervention of other variables distinct to GDP Growth, the only way is to ensure stable and high growth rates similar to those of Chile during its golden age.[208]

Nevertheless, those rates have not been sustainable and the weakness of economic growth seems to be associated with the weak influence of actual economic growth on the three analysed types of poverty. In order to analyse the evolution of the real impact of growth, we have estimated a second indicator, the growth semi-elasticity of poverty.

The interpretation of the semi-elasticity is in some aspects much clearer than that of elasticity, which refers to changes in a growth rate of poverty in relation to the GDP growth rates. Semi-elasticity, on the other hand, measures variations in the absolute

208 During the period 2006-2009, the economy was affected by a major external shock, the subprime crisis, which significantly hit the Chilean economy. This had two domestic effects. The first was changes in the net external demand for goods and services produced in the country. The second was the effect of the crisis on the global capital markets, a situation that explains variations in the exchange rate, the price of copper and inflation in energy and food. This last element was particularly relevant, since it strongly affected the disposable income of the poorest sectors of the country, limiting the impact that growth could exert on poverty, explaining why economic growth has not been reflected in a proportional reduction in poverty.

amount of poverty (variation of percentage points in relation to the variation of the GDP.[209] The expression for this kind of semi-elasticity is:

$$S\mathcal{E} = \frac{\Delta +/- \text{ Poverty (measured in percentage points)}}{\Delta +/- \text{ GDP pc (measured in percentages)}}$$

The application of this expression to the Chilean economy is reflected in Figure 6.6.

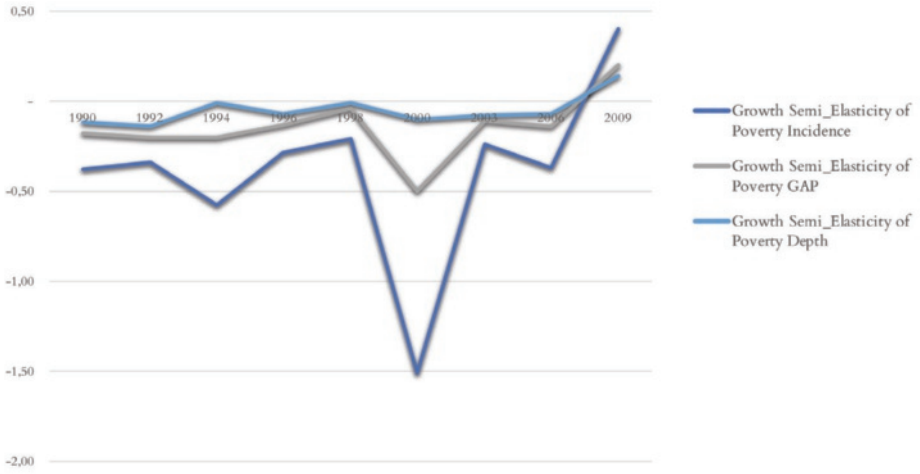

Figure 6.6. Evolution of Semi-Elasticity Growth
Source: Author´s estimations using Micro data of Mideplan-Casen surveys 1987-2009, INE population census and Chilean Central Bank.

From here, it is clear that using semi-elasticity as an indicator of poverty in relation to economic grow, we can conclude that a 1% annual increment in GDP PC will produce less than one percentage point of poverty reduction each year. With the exception of the year 2000 in which a 1% GDP PC growth reduced the poverty incidence by 1.5 percentage points, the FGT index for all the other years shows that the average impact of economic growth fits with the predictions made using semi-elasticity.

209 As Klasen and Misselhorn (2007) point out, "the number of persons leaving or entering poverty measured as percentage of the total population is clearly of more interest than the same amount measured as a percentage of the poor".

From figure 6.6, also we can corroborate which of three growth poverty semi-elasticities (calculated in a clearest way than by using growth elasticity), allows us to observe the real dimensions of poverty dependence, from the rates of output growth.

Those semi-elasticity's, in the presence of a reduction in the rate of economic growth or even when poverty increases parallel to economic growth, strongly depict in absolute terms the way in which the process of poverty reduction really behaves.

The growth semi-elasticity of poverty presents, like growth elasticity, two break points associated with the two-external shock faced by the Chilean economy during the period analysed. However, the degree of the level of poverty, before the aforementioned reduction in growth associated with such shocks, differs significantly between both measurements.

Throughout 1990-2009, the average semi-elasticity of the Headcount Poverty was only -0.4 percentage points and if the last triennium were extracted from that estimation, the average semi-elasticity would be only -0.5 percentage points.

On the other hand, the growth semi-elasticity of Poverty Gap was -0.45 percentage points for the entire period and 0.19 percentage points excluding the last triennium. Finally, the Poverty Depth semi-elasticity was 0.06 percentage points for the entire period and 0.08 percentage points if we exclude the last triennium.

The evolution of the Poverty Gap and depth of poverty reflect the simple fact that economic growth is not a real factor that drives poverty reduction during external shock periods. When economic growth loses potency; Poverty Headcount continues decreasing, and semi-elasticity increasing about one percentage point. That is the clearest indicator that the initial value of elasticity raises dramatically. However, Poverty Gap and Poverty Depth semi-elasticity (especially Poverty Depth semi-elasticity) were not seriously affected by the decline in economic growth. The Poverty Gap falls in a moderate way during the Asian crisis and rises in a similar way during the subprime crisis. In general, variations are smaller than half a percentage point. The weakened impact of Poverty Depth in relation to the semi-elasticity gap can only be explained by the wide range of social policy tools that affect both kinds of poverty and which are independent of the process of economic growth.

If we analyse data reported between 1990 and 2009 using the growth elasticity estimate, we can see that GDP per capita increments were not converted to a reduction in poverty. If instead we use estimates of semi-elasticity, we can observe in clearer way that the effect of growth, far from being transferred to poverty reduction, is filtering more than half of its effect towards other distinct purposes. We must conclude then, that independently of the kind of poverty which is being analysed, semi-elasticity let us visualise the real impact of growth on poverty within the Chilean economy in a clearer and more accurate way than the growth elasticity estimations.

6.8. Is the Chilean economic growth Pro-Poor?

In opposition to the Neoliberal perspective, some authors have suggested different ways to analyse process of poverty reduction. For instance, Dollar and Kray (2001) define that the essential issue is evaluate if the growth process is "pro-poor" or "not pro-poor". They estimate that condition using a fixed poverty line, expressed in in real value (like in Chile), which was not modifiable according to new consumption patterns adopted by persons or households whose incomes are rising. In sum, they consider that a pro-poor growth is one that is limited to allow an increasingly large number of people to exceed the poverty line.

From another perspective, authors like Kakwani (2000) declare that the economic growth is "pro-poor" only if income growth is accompanied by a change in income distribution that, by itself, may reduce poverty. From this perspective, a process of economic growth may only be defined as pro-poor if it is sustainable, including a redistribution process in which the increase of the income of the poor is transferred from the income of the richest. Thus, the absolute increase in the average income of the poor would not be "pro-poor" if unaccompanied by a reduction in inequality.

Using Dollar and Kray definition, given that in Chile there is a significant reduction in the number of poor, obviously, we would be in presence of a "pro-poor" growth, but if we use Kakwani definition, the Chilean economy does not display this kind of economic growth, because reduction of poverty has been only a relative decreasing and has not been followed by significant reduction of inequality. Indeed, measured from autonomous revenues, the income distribution has worsened. Only monetary transfers and other public goods provided by the State have achieved marginal improvements of income distribution. In short, we can conclusively say that in Chile, in any year and

for any type of measurement of poverty, the growth process exerts only a moderate beneficial effect of economic growth on poverty. That effort tends to be greater when economic growth is very high, but we can even observe a raise of poverty when rates of economic growth decrease substantially.

With elasticity of such levels as we have estimated in Chile and assuming the absence of external shocks, it would only be possible to eliminate domestic poverty if the economy again achieves GDP growth rates of at least of 6% annually. Those rates are barely achievable today (2015) when the growth rates of the Chilean economy are forecast at around 2% annually; now, it will take at least 50 years to achieve the goal of eliminating poverty.[210] That means that the neoliberal promise that achieving GDP growth rates will allow the easy elimination of poverty clearly lacks a solid foundation. Thus, we can conclude that in the Chilean case, mere growth, although it has contributed to the reduction of poverty, has done so with decreasing force. It has been following a low to moderate track in such a way that, in the long term, has been of low effectiveness in the fight against poverty.

Growth´s effectiveness in the reduction of poverty is definitively the elasticity that means the reaction of poverty when incomes change. In line with the findings of other researchers (e.g. Whitfield, 2008), our estimates of the growth elasticity and semi-elasticity seem do not explain poverty reduction as a direct function of economic growth variations. Obviously economic growth is very important for poverty reduction, but we should not forget inequality, which also affects the growth. However, even if the variable crucial for combating poverty were overthrow inequality, we could not ignore the influence of growth upon the latter.

The corollary of the favourable Chilean performance in the field of economic growth has been a significant reduction in poverty incidence. However, despite this, the evidence shows that a significant percentage of the Chilean population has only marginally exceeded the dividing line between poor and non-poor[211] then is not clear

210 That single goal can be met in relation to the definition of a given poverty line. Disappearing poverty, a result of increases in the income of households or individuals. That line will vary upwards; in such a way that there will always be a certain level of relative poverty in relation to the average income of the economy.

211 These people could easily fall back into poverty for circumstantial reasons (e.g. costly health problems, extended unemployment, etc.) or through more structural reasons linked to globalisation. For example, they could be affected by unfavourable changes in the international price of food, or if the

significance of poverty reduction However, exist an additional issue, persistence of income inequality.

That is a very complex problem and deserves separate and more detailed analysis than we already have done of the impact of income distribution on Chile´s poverty evolution.

6.9. Public Policy and Income Distribution

During the beginning of the nineties, the new elite in power had to face a tough dilemma. They had won the presidential elections in 1990 with 55% of the votes; but, they did not control the armed forces or the powerful business groups that had emerged from the shadows of the military dictatorship. In addition, they faced strong pressures from the IMF and the World Bank, which urged the new government to support the recommendations of the TWC.

In the midst of this difficult context, the new authorities needed to maintain the basic condition of their political livelihood: the unity of a coalition of seventeen political parties conducted by the right-wing Christian Democrat Party. Another significant issue was that the bulk of the voters, who had given them 55% of support, expected changes that improved income distribution, but at the same time, they did not want a deceleration of the high rates of growth that had apparently consolidated in the Chilean economy during the last five years of the dictatorship.

In other words, the challenge was not meaningful. After a short period, the new elite appreciated that their initial ambitions for transforming the overall institution associated with the Chilean Model might be hard to realise. Although they were in government, they lacked enough political power to lead a programme of real economic and social transformation, and additionally, their main economist had already abandoned the idea of implementing that kind of changes. Nonetheless, this does not mean that they simply abandoned all the distributive aims of the policies contained in their original political programme.

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economy is affected by adverse external shocks linked to the globalisation process (Contreras et al., 2005). The study of Contreras et al. shows that there is a positional high mobility in the first nine quintiles of income distribution, which means that a large part of the Chilean population is vulnerable to poverty. In other words, in spite of the sustained growth and reduction in poverty, Chile remains a country with a highly vulnerable population.

What occurred was firstly a substantial change in the selection of the instruments, through which the transformations of the model would try to be achieved, was introduced a new battery of policies and tools indiscernible of neoliberal instruments. However, as the means were not neutral in relation to the ends that they pursued, this change soon resulted in a weakening of the "willingness of change" predominant in the "Concertación", which in turn led to a new strategic course.

In fact, the government programme was gradually modified and the option as emblematic as the development of an industrial policy that let them introduce changes in primary sources of incomes, was promptly replaced by interventions from outside the productive fabric. In sum, their old program was slowly abandoned and replaced by a new one, characterised by the deployment of an "increased public spending of social orientation" (Ffrench-Davis; 2013) whose main instrument was "conditioned monetary transferences".[212]

This new policy, inspired at one time by TWC and by the programme that British New Labour began to design in the UK (McAnulla, 2007: pp.313–31 and pp.341–45; Joyce and Siesta, 2013), allowed the old idea of "rights equality" to begin to be expressed by the new Chilean leaders in a different way: "equality of opportunities" (Thatcher, 1975)[213].

This meant that the policies of successive post-dictatorship governments began to be permeated by some key elements of the neoliberal vision. As some authors analyse (Agosín et al., 2010), references to the industrial policy were discontinued and the old eighties´ emphasis on the reduction of inequality, that had been part of the discourse of the leading economists of the "Concertación, simply disappeared.

In the late-1990s a new diagnosis was established, and post-dictatorship governments no longer emphasised their old formulas that spoke of "growth with equity" (Arellano,

212 Despite this dynamic, we should note a highly relevant fact: the bulk of the Christian Democratic economists grouped in CIEPLAN, a think tank led by Alejandro Foxley, the first post dictatorship exchequer, had already ceased to believe in the need for a program of more radical economic transformation. The old programme, which had been proposed by them (Foxley, Cortázar et al., 1983), had been abandoned and in 1989, they had already subscribed, without great reserve, to the postulates of The Washington Consensus.

213 1975 Oct 10 Fr, Margaret Thatcher Speech to Conservative Party Conference: https://www.margaretthatcher.org/document/102777

2005) and about a "second phase of export lead development" (Ominami and Madrid, 1989). From this period onwards, the diagnosis was much more macro, with less emphasis on the possibilities of redeployment of public policies from microeconomics and about fostering productive development, as had been postulated from the early-1980s, (e.g. Foxley et al., 1983).

The new post-dictatorship governments soon started to believe that the more sensible option was not to implement a new industrial policy followed by strong antitrust policies, as described by Golodner (2001) and Rodrik (2004). At least throughout the first post-dictatorship government, the official policies stressed that productivity improvements and enhanced market competition must be the basis on which the "growing with equality" strategy would rest (Concertación, 1989; Minecon, 1993, Aylwin, 1994). Nevertheless, this focus was quickly abandoned (Concertación, 1994).

In a very short period, it became clear to the new leadership, that policies of redistribution aims were institutionally limited by several causes: the segregated and low quality educational system, the lack of adequate access to credit for MSMEs, the unequal and unfair rules of relationship between larger and small companies, and by the reduced size and power of the State, followed by a wide number of discriminatory public regulations that included a very regressive tax system.[214]

Surpassing those obstacles required a radical program of substitution of economic institutions defined by dictatorship, but the leadership of the new coalition government did not subscribe to that strategy. For this reason, during the second post-dictatorship government (Frei: 1994-2000), it was decided that the most "realistic" option was to limit public actions to interventions that act only over the secondary sources of income. Based on that approach, the Frei government widened the social public expenditure, firstly through implementation of CTP[215] and secondly by improving the provision

214 In general, the point of view of economists close to post-dictatorship governments aspired that social policies be equipped with larger volumes of resources than neoliberal policies utilised since 1973 to 1990. Nevertheless, during the analysed period, they also estimated that a new tax reform was unnecessary (e.g. Engel, Galetovic and Raddatz, 1998). Then, the new governments must to confront serious budget restrictions that only allow a moderate expansion of the coverage and magnitude of social policy, bigger than the ones existing pre-1990 but lower than the new authorities of social area expected.

215 In general, these CTP provide money to poor families in two ways: Conditional programmes transfer money under the condition that those transfers be used as an investment in their children's human capital, such as regular school attendance and basic preventive health care. The purpose of these programmes is to address the inter-generational transmission of poverty and to foster social inclusion by targeting the poor,

of public goods intended to elevate the minimum floor of social welfare. Obviously, both policies were focused on the low incomes deciles.

The strategy of the Government's new elite was to reinforce their own position as administrators, impelling from the State, the old extractive model which neoliberalism had created, expanded and perfected. However, this was not an easy task. The old neoliberal economic and intellectual elite had a vice-like grip on the new institutions that the new elite had already accepted as a valid rule of the game. On that basis, large business groups already administered about 80% of the GDP, ideological and cultural equipment of the country and the media.

In this context, the capabilities of negotiation of new Governments in relation to the old neoliberal elite were fragile and its greatest asset began to be one strictly electoral in nature; the ability to retain the majority support of the population. However, the maintenance of the neoliberal model starts to early on incubate a certain frustration in the population, positioning in a dangerous place their strategy. Then, the new post-dictatorship governments began to develop new social public policies, but these new programmes financed by the State maintained their neoliberal logic.

The amount spent was considerably higher than during the period of dictatorship, but the orientation was the same. The programmes of subsidies, now alleged to be of a redistributive orientation, continued to be focused on the poorest, offering economic incentives to them through monetary transfers that were not part of a programme of guaranteed social rights. On the contrary, they were framed in a neoliberal perspective oriented to focus social expenditure only in the poorest deciles of the population. In other words, after the end of dictatorship period, social policies did not undergo major qualitative amendments. The permanence of the neoliberal paradigm of the commodification of social services and resources, delivered and controlled by the government, can only be partially explained by the previously mentioned political dilemmas that the new political sector in power faced.

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focusing on children, delivering transfers to women, and changing social accountability relationships between beneficiaries, service providers and governments. Unconditional programmes are part of a rights-based approach to development. From this perspective, cash transfers are a means to ensure human rights to social protection and an adequate standard of living for all members of society, including the right to food (Palma and Urzúa, 2005). In Chile, both approaches were applied, with a clear predominance of the second one.

However, there was another explanation. When the new elite began to take control of the state, it appeared sensible for them to replace industrial policies in order to keep these kinds of programmes running given some utility criteria based on two main considerations. The first reflects the high priority that the new post-dictatorship governments placed on social policy as a mechanism selected to achieve greater equality, in the context of a market-based resource allocation system and a neoliberal institutional framework that the new authorities did not intend to modify.[216] The second one was based on the presence of an environment of economic growth, which had made it possible to increase spending, maintaining balanced public finances.[217]

The available data shows that since 1990 social spending grew rapidly and increased its importance as a compensation factor for the growing inequality that had characterised the Chilean society until the present. Indeed, during the period 1990–2009, the Public Social Spending grew much faster than GDP per capita (Figure 6.8). However, social spending rose in a very important way it did not do so in a sustained manner, because as it was affected by external shocks that weakened the State capacity to finance such expenditure. Nevertheless, government efforts should not be evaluated only by their declared orientation, or by their monetary magnitude, but by their results. Therefore, if, as we have discussed earlier, the reduction of inequality has not been significant, showing a low level of success in redistributive policies, these policies cannot be positively evaluated.

The weakness of redistribution strategies operating through public spending is the reason why many critics of the Chilean development model frequently indicate that the outcomes of the economic process of openness and globalisation present a serious social weakness (e.g. Beghin and Poitier, 1995; Robles, 2013). This criticism is expressed in relation to a series of issues in the areas of income inequality, high levels of pollution, regional disparity, low productive diversification and low productivity.

216 A basic rule of the game that to date has not been questioned by post-dictatorship governments is the definition of the Chilean state as one that plays a subsidiary role in the economic sphere. It is worth saying: this does not include any economic activity able to be developed by the private sector. It is not possible to modify this definition, which is part of the Constitution of 1980, without a radical constitutional change.

217 That second consideration was an economic condition highly validated by new authorities that, especially during the first year of transition to democracy, were looking for a new equilibrium between political and economic stability and grassroots political support.

These problems cannot be fully addressed from the social policy perspective alone. On the contrary, they require setting up more inclusive institutions, whose absence casts real doubt on the modernisation process that Chile has experienced in the last thirty years. This point of view has been emphasised from different angles by various authors (Sunkel, 1995; Vos and Paes de Barros, 2002; Gustafson and Pattnayak, 2003; Green, 2003; Huber and Solt, 2004; Taylor, 2006; Kharas, Leipzinger et al., 2008; OECD, 2009). However, a more detailed appraisal of this situation requires a wider analysis of the institutions which define the presence of a weak market competition, and which determine relations between capital and labour, between sizes of companies and also the general specialisation of the economy - all of those factors are extremely relevant to our analysis.

It seems clear that, although Chilean social expenditure has raised the absolute level of incomes for disadvantaged groups, this increase has not been enough to reduce the income inequality produced within the labour market. In fact, throughout the period 1990 to 2009, labour incomes represented more than 90% of autonomous income[218] and precisely this high percentage explains why, in the analysed period, inequality would have increased. If enterprises, particularly large companies that generate the bulk of the GDP and (in 2009) 37% of formal employment, do not generate primary incomes that improve the labour remunerations, it is very unlikely that this gap- consisting of a certain kind of "Ricardian rents of capital"- can be compensated by a program of monetary transferences (CTP).

That is the reason why the considerable growth of the Chilean economy has not translated into a similar impact on the reduction of poverty or much less a decline in inequality, because, as we will show below in Figure 6.7, the reduction of poverty and the reduction of inequality, have not operated in Chile as simultaneous phenomena. In the Chilean case, lower levels of poverty seem to coexist with higher levels of inequality in such a way that the distribution of autonomous incomes is strongly concentrated in the top quintile of incomes.

218 Labour incomes are 1) incomes earned by workers in their main occupation in the form of wages, 2) Profits from capitalist and self-employment and 3) Auto-provision of goods produced by households. The autonomous income also includes others' incomes consisting of bonuses, rents, interest, as well as retirement, pensions, and transfers between private and monetary allowances received by public employees.

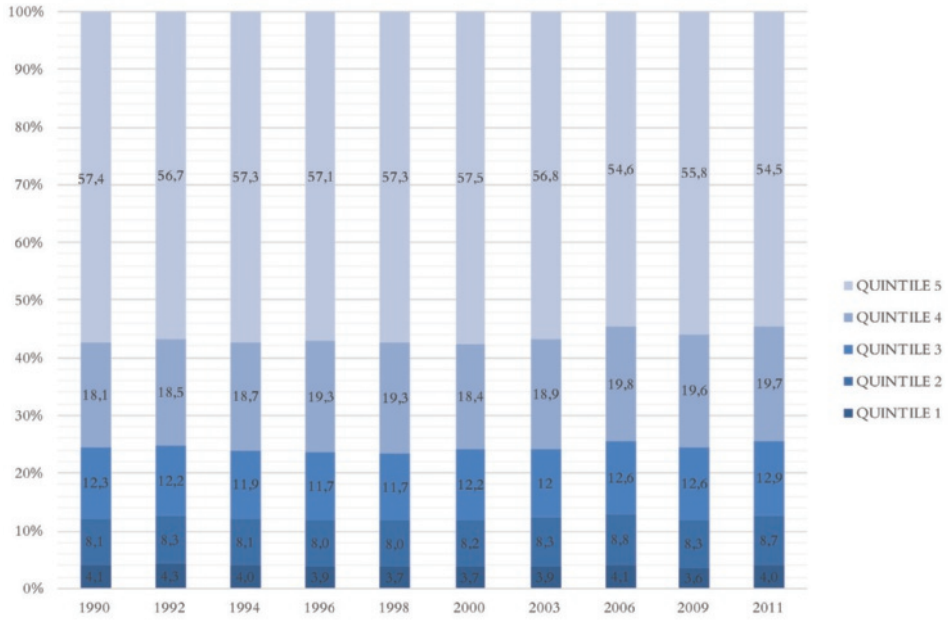

Figure 6.7. Distribution of Autonomous Income Per Capita of Households by Quintiles of Income
Source: Author´s elaboration based on information provided by the CASEN surveys 1990-2009, using the official concept of autonomous household per capita income of Chilean Ministry of Social Welfare (Mideplan, 2010).

At first glance, figure 6.7, clearly shows that between 1990 and 2009 the participation of the richest 20% of the Chilean population decreased slightly, from 57.4% to 54,5% of autonomous incomes. Especially, the top quintile (the richest 20% of the population) slightly decreased their income share (by 2.9 per cent). On the other hand, the two poorest quintiles, improved their participation in the total income of households by only a small amount (0.5 per cent). Both figures do not significantly modify the pre-existing levels, up to 1990, of income concentration and inequality. On the other hand, the autonomous income of poorest families (bottom quintile), fell from a perceived 4.1% to 4.0%. That is a lower proportion than twenty years ago, and a situation indeed quite different to what was expected if we consider that during the last twenty-five years Chilean GDP grew 2.5 times (BCCH, 2015).[219]

219 The CASEN surveys analysed in this research only partially describe this situation. People tend to under-declare their income in the household's surveys, especially those of the highest revenue decile, in such a way that even a disaggregation of the results of these surveys in quintiles would not be enough to show the real dimensions of the concentration in a small group of people and families. If one compares the two quintiles of higher incomes with the two lower-income quintiles, it can be observed that whilst the participation of the top quintiles declined from 75.5% in 1990 to 74.2% in 2009, the poorest quintiles rose from 12.2% in 1990 to 12.7% in the same period. The richest quintile of the population earned an

This trend was maintained without any major changes from 1990 onwards because, throughout the twenty years of liberalisation analysed in this research, rarely did the share of the poorest quintile exceed 4% of total autonomous incomes of total households and persons. This situation was slightly modified during the period between 1990 and 2009, and only due to the increase of monetary income of families through programmes of cash transferences (CTP), whose magnitudes are displayed in Figure 6.8.

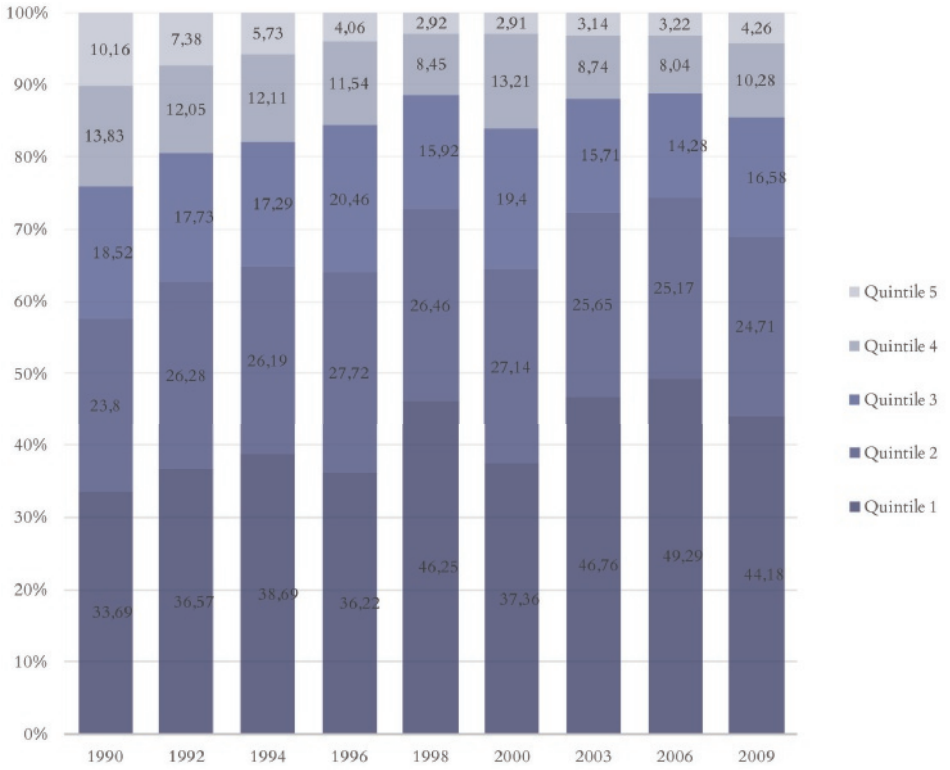

Figure 6.8. Distribution of Monetary Subsidies by Quintiles of Autonomous Incomes
Source: Author´s elaboration based on information provided by the CASEN surveys 1990-2009, using the official concept of autonomous household per capita income of Chilean Ministry of Social Welfare (Mideplan, 2010).

income 6.2 times greater than that earned by the poorest quintiles in 1990. In 2009, they earned an income 5.8 times larger than the poorest quintiles. If the figures are expressed in deciles, in 1990 the richest decile earned 14 times more than the poorest decile and in 2009 that situation remained almost unchanged. Controlling the income sub-statements, the inequality would be even bigger.

The effect of that CTP that the different income quintiles receive from the State, whose amount and distribution is displayed by Figure 6.9, slowly improved the distribution of income.

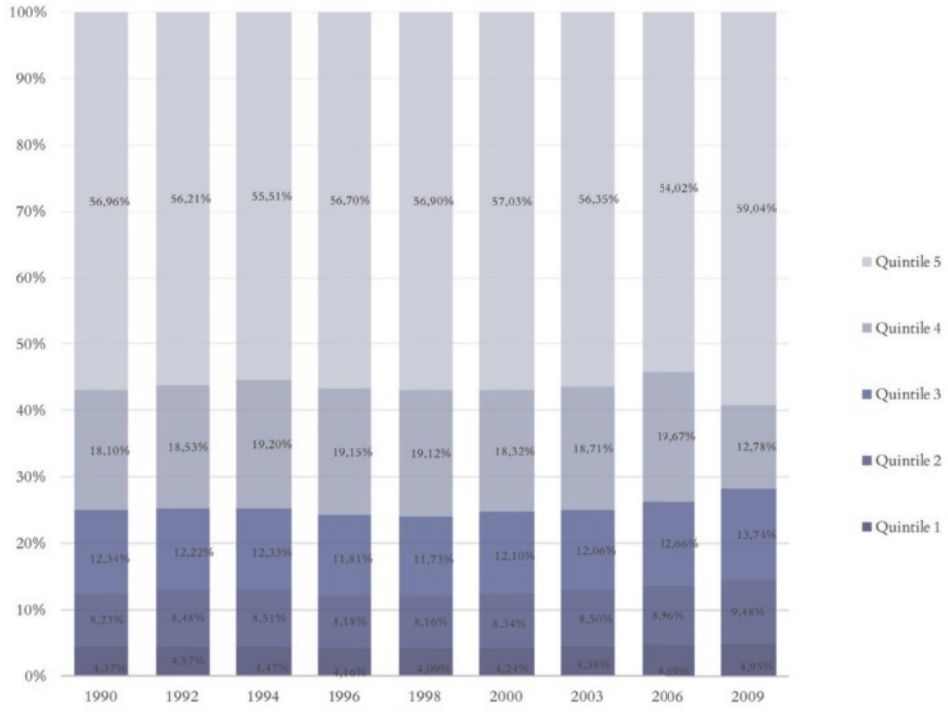

Figure 6.9. Chile: Distribution of Household Monetary Incomes by Quintiles
Source: Author´s elaboration based on information provided by the CASEN surveys 1990-2009, using the official concept of autonomous household per capita income of Chilean Ministry of Social Welfare (Mideplan, 2010).

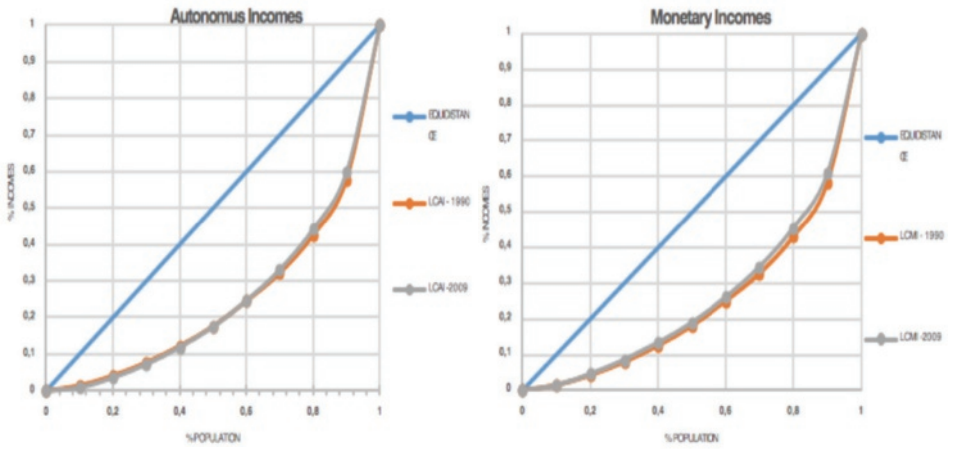

Figure 6.10. Lorenz Curves Income Distribution: 1990–2009.
Source: Author´s elaboration based on information provided by the CASEN surveys 1990–2009.

However, as it is also showed in Lorenz curves of autonomous and monetary incomes (graphed in Figure 6.10), in Chile the income of the wealthiest differs greatly from the income of the rest of the population. That is true even when the poor´s autonomous incomes have been complemented by a significant amount of monetary and non-monetary transfers. In fact, from that figures, we can deduce that large magnitude of income differences between the rich and the poor strata in Chilean society, as well as their persistence over time, makes it unrealistic to expect an improvement in income distribution based on trickle down plus public policies, mainly based on CTP.

Social policy is one redistributive instrument whose aim is to improve people's standards of living. As next Figure 6.11. below shows, Chilean this was oriented to social groups with limited resources in the Chilean case, adding to household incomes and subsidies for health, education and housing, as well as money transfers, amongst other things. It was through these measures that redistributive policies based on direct subsidies to the poor were implemented.

Based on this approach, from the early 1990's the post dictatorship governments quickly increased the amount of total public spending per capita (Arellano; 2005, 2012). Within it, social spending grew in a higher proportion, so that the increment in the areas of education and health was particularly significant.

From 1990 to 2006, the social expenditure per capita growth was less than GDP per capita growth, but since 2007, it has grown beyond GDP per capita. In less than a

decade, within Chilean public policy issues of income distribution ceased to rise in a way that was linked to programmes which foster the ability of enterprise to generate income improvement, which would allow them to increase the salaries paid to their employees.

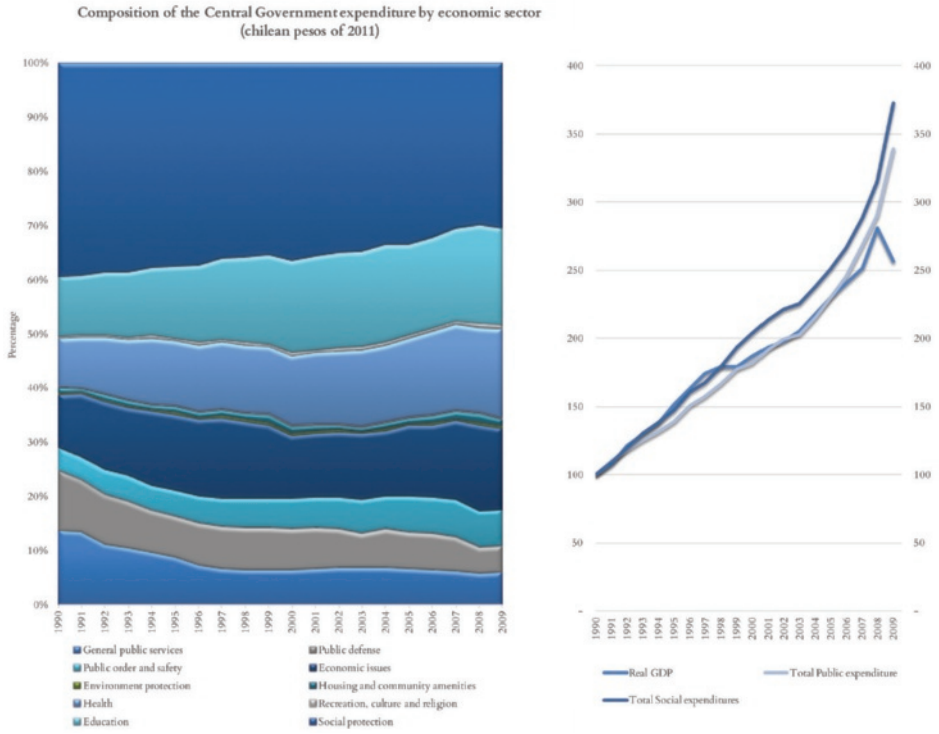

Figure 6.11. Social Public Expenditure. Chile 1990–2009.
Source: Author´s Elaboration Using Figures of DIPRES. Ministry of Finances. Statistic of Public Finances, Figures in Pesos of 2001 (A) and 1990 (B).

Therefore, increased expenditure does not necessarily imply a distributive improvement. To achieve this, it is necessary to prevent the leakage of such expenditure to the wealthier sectors, as well as the use of public resources in programs of low distributive effectiveness. For that reason, it is necessary to consider the real impact that growing social expenditure has on the total income per capita, for proper measurement of income distribution and to prevent inequality being magnified, despite increases in public social expenditure.

Unlike autonomous income, monetary income includes transfers and subsidies from the state, and when the Gini Coefficient is estimated based on monetary incomes we observe a small improvement in estimates based on autonomous income.[220] This reflects the existence of a certain positive impact on income distribution exercised by monetary subsidies provided by the Chilean governments, but this impact is not very significant in relative terms.[221] In fact, the Gini Coefficient and the remaining

220 The Gini is the most commonly used measure of inequality. This index measures to what extent the income distribution amongst individuals or households within an economy deviates from an equal distribution. From the Lorenz curve, which shows the cumulative percentages of total income received against the cumulative number of receivers (starting from the person or the poorest households), the Gini coefficient measures the area between the Lorenz curve and a hypothetical line of absolute equality, expressed as a percentage of the maximum area under the line. The Gini coefficient is widely used since it is more sensitive to changes in income that occur in the middle of the distribution, but it is not the only inequality indicator. Frequently income distribution is examined using other tools to which are considered more useful in dealing with the gap at the top and bottom segments of the income scale.

221 The major subsidies that were part of the monetary transfers implemented by the Chilean state are the following. Single Family Benefit (SUF): The SUF is defined as the benefit equivalent to the first stage of family allowance, for people with limited resources who are unable access any other subsidies available by law since they are not dependent workers affiliated to a pension system. Those who can apply for this benefit must be under the age of eighteen or be disabled people of any age, who live at the expense of the recipient. Also eligible are: mothers of children who live at their expense. Pregnant women. Persons (of any age) with a deficit in their mental capacities, who are not beneficiaries of the mental disability grant. Disabled people of any age, mothers of all infants or in their absence, the fathers, the guardians or others raising the child and persons who are caring for the mentally disabled. Maternal and family allowances. Beneficiaries of the family allowance are: (i) Workers dependent on the public and private sector. (ii) Independent workers affiliated to a regime of foresight that on January 1, 1974 received the Family Allowance (beneficiaries of land reform, taxi owners and newspaper hawkers). (iii) Workers that are receiving subsidies of any kind. (iv) Workers identified in items one and two that are pensioners through any welfare system, even when in the respective schemes, they have not been entitled to the benefit. (V) Beneficiaries of widow's pension and mothers of children of the worker or pensioner receiving a special pension (vi) Institutions of the state or state-recognized by the government to keep disabled, orphaned or abandoned children, (vii) people who are caring for children by judicial resolution. Subsidy of the cost of the consumption of drinking water, sewerage and wastewater treatment (SAP): This consists of financing by the state of a proportion or percentage of the monthly payment of a maximum consumption in cubic meters of potable water and sewerage to residential users of scarce resources. Subsidy for Mental Disability: consists of a monthly pecuniary benefit of equal amount for all beneficiaries. Family Protection Bonus: is a monetary contribution to families involved in the "Chile Solidario" system, which is given for a maximum period of twenty-four months (two years). Basic Solidarity Pension (ex PASIS): is a monthly monetary benefit, covered by taxes, which can be accessed by all those who do not have the right to a pension in some welfare system and who fulfil the requirements specified by law. It is intended for people of sixty-five and older who do not have the right to a pension in some welfare system. Solidarity of Disability Pension (ex PASIS disability): is the benefit funded by the state to people declared disabled who do not have the right to a pension in some welfare system, either as owners or as beneficiaries of a survival pension. Subsidy of

indicators of inequality (which are outlined in Table N° 6.1) remain at a high range despite these subsidies.

The bulk of policies implemented in Chile throughout the openness process, contradict the optimistic predictions of several authors using neoclassical tools (e.g. Alesina, A., E. Spolaore, and R. Wacziarg 2000) who assume the materialization of a progressive income distribution as a result of trade openness. These projections, using the figure of the two decades analysed in this study as contrast, seem to only be wishful thinking. Chile, despite being an open and globalised economy, did not seem to show a tendency to significantly improve the relative situation of the poorest based on their insertion into the productive fabric (autonomous incomes), the place where the bulk of personal and household's incomes are produced.

Moreover, if we analyse the evolution of autonomous income distribution, we can clearly observe that the distributive situation of the very poorest, in relative terms, has slightly worsened, in spite of the enormous progress that the Chilean economy made during 1990-2009 in terms of growth, globalisation and poverty reduction. This means that, after thirty-four years of drastic trade liberalisation (1976-2009), the fruits of the Chilean growth and globalisation process have not been redistributed in a fair way.

6.10. The Roots of Income Concentration

In Chile, income concentration is not a recent phenomenon. The actual levels originated from the dictatorship, but the concentration's roots are far older. The presence of a regressive distribution of income has been present for over two hundred years of Chilean history and it would not be fair to attribute its origins only to the dictatorial regime that governed Chile between 1973 and 1989. However, during the dictatorship period, a significant worsening of income distribution took place, installing greater regressive income distribution than the distribution installed before it and that had been improved during the short time that the government of Salvador Allende had remained in office.

Unemployment: is aid of an economic nature, which is awarded to workers who have lost their jobs and comply with other legal requirements indicated, for a maximum period of three hundred and sixty days. One-time subsidies: another way that has been designed to increase incomes, especially for those lacking in resources, is through the granting of bonuses that are granted once and at certain times of the year.

As we can see in Figure 6.8, during the only period of import substitution for which exist systematic information about incomes exists (1957–1973), the distribution of it was far away from ideal.[222]

Between 1957 and 1973, three different governments administered Chile. Jorge Alessandri ruled between 1958 and 1964, supported by a coalition of right-wing parties and with strong support from the economic world. In Figure 6.8, we can see that during the period of this conservative government, who began its administration with a 0.44 Gini coefficient, levels of income inequality were relatively low for Chilean standards (the Gini of the period was 0.45 on average). Between 1957 and 1973, three different governments administered Chile.

President Jorge Alessandri ruled Chile between 1958 and 1964, supported by a coalition of right-wing parties and with strong support from the business world. In Figure 6.12, we can see that during the period of this conservative government, who began its administration with a 0.44 Gini coefficient, levels of income inequality were relatively low for Chilean standards (the Gini of the period was 0.45 on average).

The next government was ruled by the reformist Christian Democrat, Eduardo Frei Montalva. During this government, the Gini Coefficient rose from 0.46 to 0.49 (the Gini of the period was 0.47 on average).[223] The Christian Democrat administration was followed by the socialist government of Salvador Allende (1970–1973), interrupted by a coup in 1973 that established seventeen years a harsh military dictatorship (1973–1990).

The government of Salvador Allende was a period in which Chile began a transition to socialism that was characterised by a sharp drop in levels of inequality (the biggest in the Chilean history). The Gini coefficient fell from 0.49 to 0.45 (the Gini of the period was 0.47 on average) pari-passu the policies of expansion of aggregated demand and income redistribution which were aggressively applied at the time.

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222 During the period 1957-1990, there were lesser degrees of inequality than those latterly registered in the post-dictatorship period (after 1990). During the sixties, the participation of the poorest income decile fluctuate around 1.5%. The richest decile had a participation of 40%. The five poorest deciles absorbed around 17% of the wealth of the economy, while the richer five deciles captured more than 83%. (Eskia, 1967).

223 Such increase to the levels of inequality draw attention because a series of changes of redistributive nature were introduced at that time, such as the massive unionisation of the urban and rural labour force, agrarian reform and the increase in social spending.

This redistributive effort caused strong monetary and fiscal imbalances that led to hyperinflation and to high levels of political and social conflict. All these factors fuelled the deep fracture in Chilean society already described, and culminated in the bloody coup d'état and a right-wing military dictatorship which ruled Chile between September 1973 and March 1990.

As previously described, the military dictatorship implemented strong trade openness and market liberalisation, moving from a strategy based on import substitution towards a market-oriented export model.[224]

During this period, as Figure 6.12 shows, income inequality rose parallel to the trade openness and liberalisation of the Chilean economy. As we can see in this figure the evolution of Gini Coefficients during the twenty years' period under analysis (1990-2009) contains a set of heterogeneous sub-periods in which different public policies were implemented. Nevertheless, in general, the distributive situation did not originate in the, but mostly originated in the periods prior.

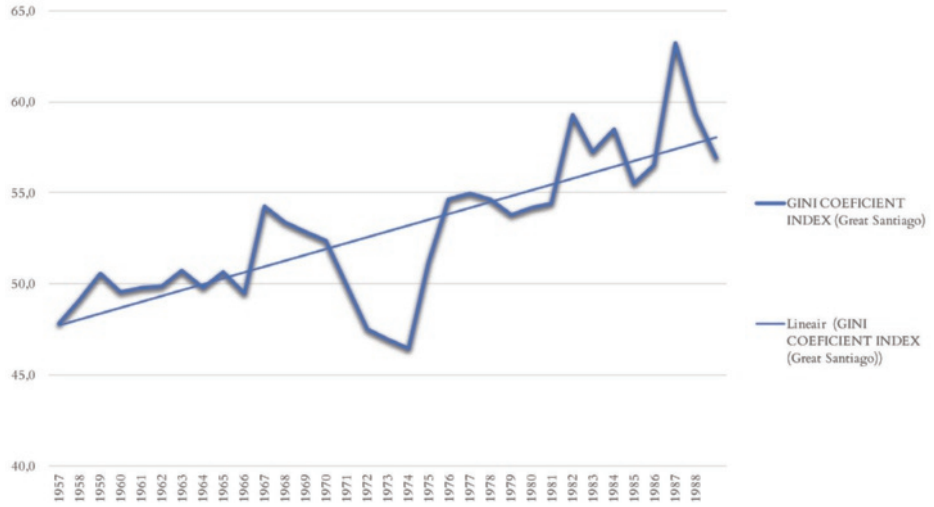

Figure 6.12. Evolution of Income Distribution: Chile 1957-1989.
Source: Authorial elaboration based on data base from Surveys by the Department of Economics, the University of Chile.

224 The distribution of income in this period, shows a clear trend towards greater inequality, which is synthesized in the increase of the Gini Coefficient from 0.45 to 0.57 (the Gini of the period was on average 0.56), generating in 1987 the highest level of inequality (0.63) registered for Chile throughout the fifty-four years covered by University of Chile data.

However, stagnation of inherited income distribution is a result of post-dictatorship public policies. Because between 1990 and 2009, the economy experienced a period of high GDP without modifications on their former income distribution. The option selected to improve income distribution was a strong expansion of social spending, to impulse the achievement of social equity, alongside the deployment of a process of economic growth. An important part of the government's programme of post-1990 administrations was to recover Chile's condition prior to 1973 when, along with Uruguay and Argentina, it had been one of the countries with the lowest levels of relative inequality in Latin America, a continent of high levels of inequality. However, as we can see in Figure 6.13, income inequality during the post-dictatorship period has followed a slow and fluctuating path of recovery from the distribution existing prior to the period of military dictatorship; it should be noted then, that trade openness and its outcomes have not been noteworthy in this respect.[225]

Although the first phase of the liberalisation of the Chilean economy was not characterised by significant improvements in growth rates, since the middle of the 1980s, and steadily from the beginning of the 1990s, Chile has registered growth rates of GDP (total and per capita) well above its historical average.]

225 In the post-dictatorship period, 1990 to 2009, a political coalition of centre-left parties came to government four times (1990-2010), the first two administrations led by Christian-Democrat presidents and the last two by Socialist presidents. However, domestic income distribution has experienced only a slight improvement and its evolution has been erratic. From 1990 to 1994, as Figure 6.9 shows, Chile´s income distribution improved significantly, and then worsened significantly, from 1994 to 2000. It improved again until 2004 and worsened again until 2009, showing high discontinuity with weak and intermittent tendencies. By using this data, we can observe that the only presidential term in which there was a positive and significant correlation between growth and inequality reduction produced from implemented public policies was the first post-dictatorship government of Patricio Aylwin, (1990-1994). The next government, led by Eduardo Frei Ruiz-Tagle (1994-2000), was characterised by a context of slow growth, high unemployment and low inflation, generating a serious deterioration in income distribution. In the area of income distribution, the situation of the country returned to the same status quo that existed towards the end of the military dictatorship. During the third post-dictatorship government of Ricardo Lagos (2000-2006), the weakened income distribution improved four points during its first three years in office, remaining constant during the fourth year, and worsening again during the last year. In summary, income distribution improved only one point in relation to the situation inherited from the Frei administration. Meanwhile, during the first and second years of the fourth government led by Michelle Bachelet (2006-2010), the situation of income distribution improved seriously (from a Gini of 0.54 to 0.51), but then worsened again and Chile virtually returned to the income distribution that characterised the country in 1995 (0.53).

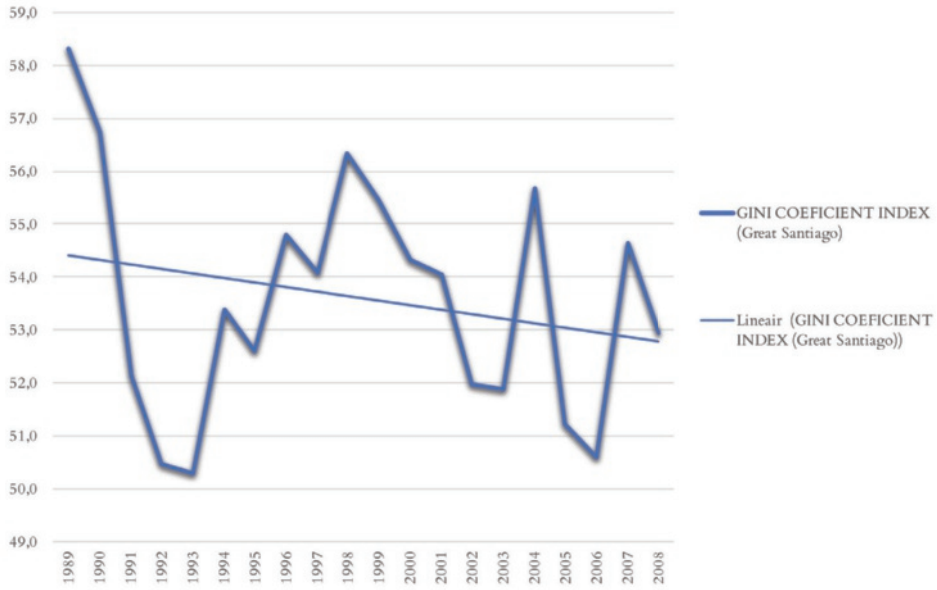

Figure 6.13. Evolution of Income Distribution: Chile 1990-2009.
Source: Author´s 'Elaboration based on data from surveys of Department of Economics, University of Chile.

In effect, the Chilean average GDP rate of growth throughout the period of 1990 to 2009 was close to 5.08%. Yet these positive figures, which have led the Chilean GDP to almost triple in twenty years, have not significantly impacted income distribution. this has not only been due to the fact that no attempt has been made to alter the primary distribution of income. Additionally, the State intervention and its tendency to modify only the secondary income, through a battery of monetary subsidies, has not been efficient in addressing the strong income inequality exhibited by the Chilean economy.

6.11. The Measurement of Inequality

Among the multiple indicators proposed in the literature focused on inequality issues (Atkinson & Piketty, 2010), in our opinion, there are at least three that can be particularly useful to our research: (Index D10/D1); (D10/D1-D4) and (D9-D10/D1-D2). But we also use another three additional indexes Gini, Kawani and Raymond-Smolensky indexes.[226] We will estimate all these indexes using primarily autonomous incomes data, and then monetary incomes data.

226 In this case, the figures have been presented in deciles in order to give a more precise idea of income

Table 6.1. Income Distribution Coefficients

AUTONOMOUS INCOMES									
YEAR	1990	1992	1994	1996	1998	2000	2003	2006	2009
Index D10/D1	30,5	28,1	30,9	33,0	34,7	34,2	34,4	31,3	46,0
Index D10/D1:D4	3,5	3,3	3,4	3,5	3,5	3,5	3,4	3,0	3,4
Index D9-D10/D1+D2	14,0	13,2	14,0	14,8	15,6	14,5	14,5	13,1	15,7
Gini Autonomous Incomes Index	0,6	0,6	0,6	0,6	0,6	0,6	0,6	0,5	0,6
MONETARY INCOMES									
Index D10/D1	27,1	25,2	27,7	28,7	28,4	29,5	27,3	23,9	25,9
Index D10/D1-D4	3,3	3,2	3,3	3,4	3,3	3,3	3,2	2,8	2,9
Index D9-D10/D1-D2	13,0	12,3	13,1	13,6	13,9	13,3	12,8	11,5	11,9
Gini Monetary Incomes Index	0,6	0,6	0,6	0,6	0,6	0,6	0,6	0,5	0,5
Quasi Gini Monetary Transferences	0,2	0,7	1,3	0,3	0,4	0,3	0,4	0,5	0,4
Kawani Index (%)	-0,3	0,1	0,7	-0,2	-0,1	-0,2	-0,1	-0,1	-0,1
Raymonds Smolensky Index	0,009	0,001	0,020	0,013	0,008	0,002	0,010	0,008	0,023

Source: Author´s elaboration using CASEN surveys information[227].

1. The D10/D1, ratio will be the income share of the richest 10% of the population divided by the income share of 10% of poorest population. This ratio compares two parts of the income distribution, rather than the distribution as a whole; equality between these parts corresponds to 1:1, while the more unequal the parts, the greater the ratio. Contrarily to Gini coefficient, this ratio only measures changes in the distribution of income if it either affects the 10% of the population with the lowest incomes or to the highest 10% earners and therefore relates better to the common understanding of inequality.
2. The (D10/D1-D4) will be the income share of the richest 10% of the population's (D10) divided by income share of the poorest deciles (D1+D2+D3+D4).
3. A third indicator is the ratio (D9+10/D1+D2), established between the two upper deciles and the two lower, an indicator of widespread of inequality that

distribution by socio-economic stratum.

227 From 1990 to 2009, the lowest income decile (D1) falls from 1.4% of total income to only 0.9%. During the same period, the higher decile falls from 42.2% of total income to only 40.2%.

is easy to interpret and similar to the /D10/D1) ratio, but using quintiles in place of deciles.

Using primarily autonomous income data to estimate that three indexes and then monetary incomes, we obtain interesting results.

In first place, we estimate the (D10/D1) ratio using autonomous incomes, we can see that the people from the higher income decile, in 1990 possessed an income level more than thirty times the income of the lowest decile. When we use monetary incomes to estimate the same index, we find that the top decile has twenty-seven times the income of the lowest decile, conveying in both cases a sharp picture of concentration.

Estimating (D10/D1-D4) index using autonomous income data, we can see that in 1990, incomes of the richest 10% of the population were 3.5 times the aggregate income of the four poorest deciles. In 2009, this declined a small amount, representing 3.3 times the income of the four poorest deciles. If the same index is estimated using monetary incomes, the richest 10% of the population were 3.3 times the aggregate income of the four poorest deciles, a minor difference to first estimation.

Lastly, if we estimate the (D10/D1-D2) coefficient using autonomous incomes, we can see that in 1990 incomes of the top deciles versus were fourteen times the incomes of the bottom deciles. In 2009, the ratio shows a difference of sixteen times between the two groups of income deciles. When monetary incomes are used, the 1990 ratio is thirteen times, and in 2009 twelve times. In sum, the indexes fluctuate some depending on the kind of income used to calculate it but remain very similar.

The small but positive effect of government action on equality, operating throughout subsidies, has been exerted along several routes, which aimed to compensate the poor income distribution produced by the regressive arrangements in production area and in labour markets, is the base in which are build inequalities existing in Chilean markets and from there, bad income distribution.[228]

228 That is an issue to be analysed in a more detailed way in the next chapters.

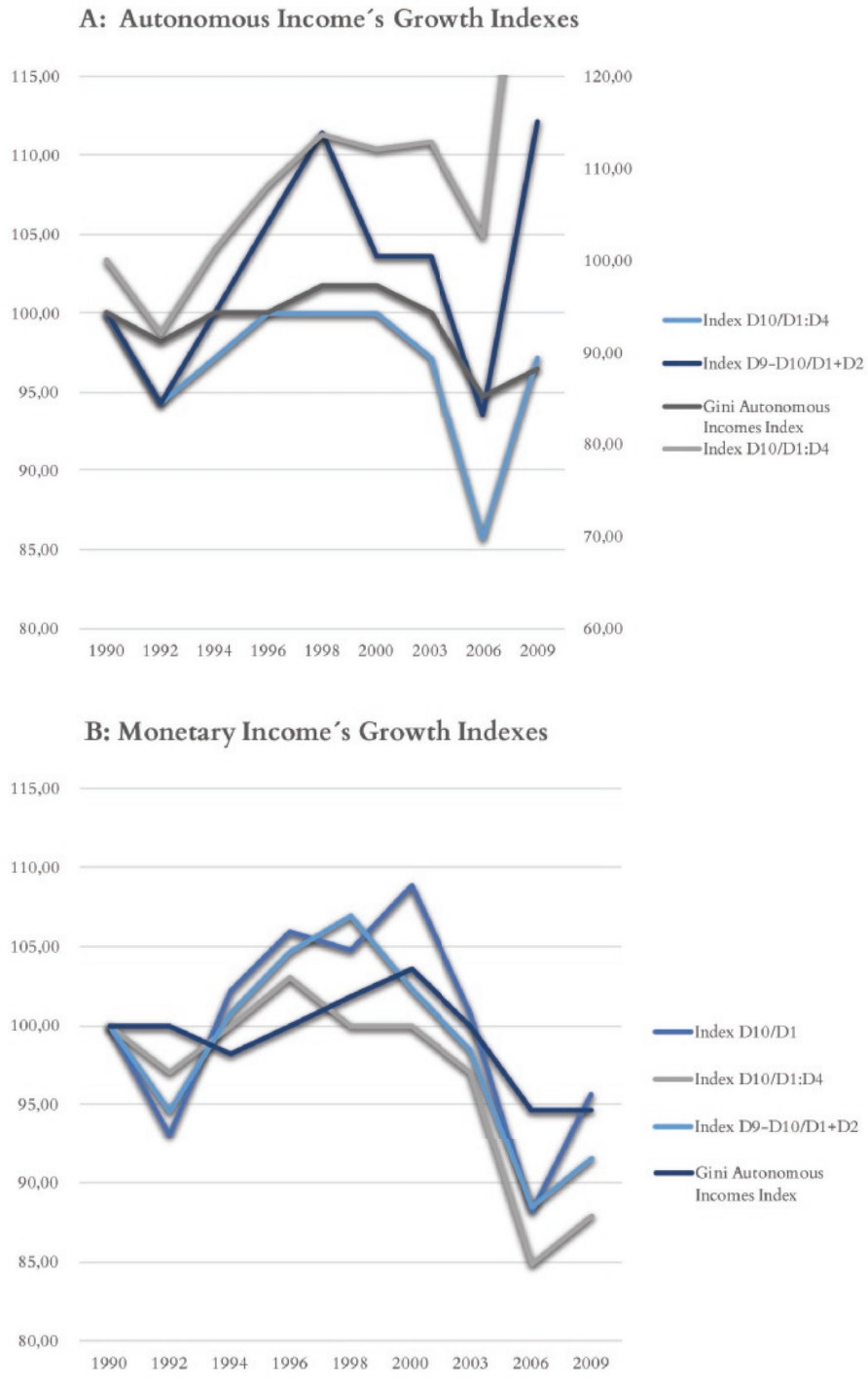

Figure 6.14. Comparative Measurements of Income Distribution Evolution. Chile 1990-2009. Source: Author´s elaboration using CASEN surveys information.

There are various other indicators, but, in our opinion, the three indexes contained in Table 6.1 and figure 6.14, provides a first glance of the Chilean economic trends of income distribution.[229] Jointly they inform us that in 1990 the income distribution was very regressive, independently of index used to estimate it. Nevertheless, despite twenty years of openness and liberalization, followed by greater levels of GDP and productivity claimed by neoliberal as related to better income distribution and higher remunerations, the inequality between the richest and the poorest has remained stable. In fact, in 1990 the richest population decile (D)+D10) concentrated 57% of autonomous income, whilst the remaining nine deciles, as a whole, captured the remaining 43%.[230] In 2009, twenty years later the richest decile captured 56% of autonomous income, and the remaining deciles 44%.

The evolution of the three ratios shown in Figure 6.15. confirm that in Chile concentration of income remains without major variations, whatever that government's actions. The monetary subsidies decrease the inequality gap, but do not modify it significantly given that sources of autonomous income remain unaltered.[231] However, the cited indexes describe inadequately the current relationship among the delivery of monetary transferences and redistributive capacity of these policy instruments.

Addressing these issues requires use additional indicators. We select two devices in order to develop that analysis. Ones is the Kakwani index (K), which is based in turn

229 Casen Survey presents a difficulty: their results are ex-post adjusted to the values of the Chilean National Accounts. Given the methodological problems associated with this option, the mean household incomes per capita derived from the CASEN survey differ from the level incomes per capita derived from national accounts. Growth rates estimated from these two sources can differ as well. Given that estimates differ substantially, it is sound to presume that one is better than the other is; even both data sources are susceptible to errors. To use both data when available, and afterwards determine that the extent of the discrepancies is recommended as good practice (Ravallion, 2001; Deaton and Kozel, 2005). In Chile, it is not possible to re-estimate results from 1990 to 1998, but it is possible from 2000 - 2009. Unfortunately, taking that option would force us to analyse only a portion of the period under study. To analyse joint series with different methodologies is not possible without affecting the conclusions drawn. From 2013 onwards, Mideplan estimated CASEN results without adjusting their data to the national accounts.

230 From 1990 to 2009, the lowest income decile (D1) falls from 1.4% of total income to only 0.9%. During the same period, the higher decile falls from 42.2% of total income to only 40.2%.

231 Although the Gini coefficient decreased from 0.56 to 0.53 during that period, all Chileans (including the poorest) improved their absolute income. Nevertheless, due to popular rejection of this slight relative improvement in income, the centre of the national political discussion has become income distribution.

on the Gini index, allowing, in this case, indicate the progressivity or regressivity of subsidies (monetary transferences) to the poorest deciles.

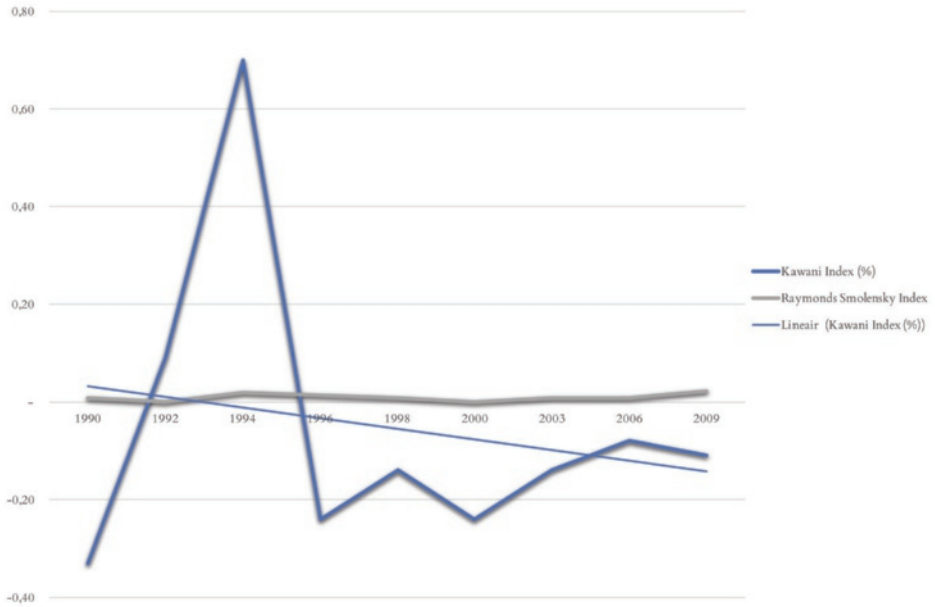

Figure 6.15. The Kakwani and Reynolds-Smolensky Indexes Evolution.
Source: Author´s elaboration from Case Data.

The Kakwani is the difference between the Quasi Gini index of the transferences curve and the Gini index of the pre-transfers income´s situation. However, this index is not influenced by the absolute value of incomes, and then tells little about incomes redistribution. For example, applied subsidies could be strongly progressive, but if its absolute amount is irrelevant its character may be regressive.
Therefore, generally the analysis of progressivity of public spending is complemented whit Reynolds-Smolensky index (RS), a global indicator of the redistributive capacity of the subsidies (transferences) in question. If Kakwani index $K > 0$, means that transferences are progressive (contributes to reducing inequality in the distribution of income).

If $K < 0$ means that monetary transferences are regressive. On the other hand, the Reynolds-Smolensky index (RS) is defined as the coefficient Gini before monetary transfers, less the Gini index, estimated for incomes after transferences, by measuring

how well change the inequality of incomes (in terms of the Gini points) as a result of the introduction of a battery of monetary transferences (or taxes). Then, if Reynolds-Smolensky index RS < 0, means that transferences are progressive (contributes to reducing inequality in the distribution of income). If RS > 0 means that monetary transferences are regressive.

Figure 6.15. and Table 6.1 (given the values of K and RS indexes) show a situation clearly regressive. In spite of the first years after the end of the dictatorship, in which a tax reform lets deployment of a new battery of social programs that produce a progressive effect, from here in advance the monetary transfer does not give a real support to any redistributive program. The impact of subsidies policies exists, but is so weak and does not explain the bulk of the extremely reduced income distribution.

The Chilean public policies and, more in general, the whole discourse of the State, has been very careful avoiding to confront these issues, limiting itself to declare that their battery of monetary subsidies tends to improve the situation of the poorest population. As a consequence, regressive of that course of action, incomes distribution inherited from dictatorship has remained without mayor changes during the twenty analysed years. The meagre distribution of income in Chile, who is relatively impervious to subsidies oriented to improve it, is produced by high income´s concentration in the tenth decile, which encompasses the richest people in the country. Without modifying that level of concentration, it will be very difficult modify, in an enduring and progressive way, income distribution. This situation is widely displayed in Table 6.2. that shows the dispersion of incomes between different deciles of incomes during the analysed period.

Table 6.2. Standard Deviation of Income Distribution using Gini Index, with and without Richest Deciles

	1990	1992	1994	1996	1998	2000	2003	2006	2009
					Autonomous Income				
A-I: Devest 10 Deciles	12,01	11,84	11,91	11,94	11,87	12,08	11,82	10,94	11,45
A-I: Devest 9 Deciles	4,18	4,31	4,37	4,62	4,41	4,34	4,56	4,47	3,29
A-I: Devest 8 Deciles	2,65	2,66	2,75	2,93	2,93	2,66	2,77	2,87	2,93
					Monetary Income				
M-I: Devest 10 Deciles	11,89	11,72	11,25	11,78	11,71	11,92	11,64	10,72	11,03
M-I: Devest 9 Deciles	4,11	4,38	4,32	4,54	4,32	4,24	4,44	4,29	3,07
M-I: Devest 8 Deciles	2,61	2,62	2,77	2,84	2,85	2,59	2,68	2,77	2,76

Source: Author´s elaboration using CASEN surveys information.

In that table, we can see the standard deviation of incomes, a measure of dispersion of the incomes perceived by the different deciles of Chile´s population, in relation to the average income of the economy. Subsequently, the table displays how, if we eliminate decile 10, the standard deviation of income falls drastically, and if we eliminate deciles 10 and 9, income distribution falls further. This means that, in the absence of the influence of the two richest deciles (the top quintile), the income dispersion around the average income looks very similar to that of the OECD developed countries.

This situation shows that a key fact of the income distribution in Chile is the hither to analysed impact of the richer quintile and especially influence of richest decile on the distribution of income.[232]

The outcome of applying State´s intervention programs that do not modify autonomous income distribution has been that, after twenty years after the end of the dictatorship, the distribution of income in Chile (reflected by the "monetary incomes Gini" of 0.53) was only one point less than the average Gini of the whole dictatorship period 1974–1989 (0.54). This situation is not only displayed in the evolution of the Gini Coefficient of Greater Santiago[233]: The estimation of Kakwani and Reymond-Smolensky indexes, complementary show the infectivity of monetary transference system by means the Chilean government has been trying to improve income distribution.

6.12. The Efficiency-Equality Trade Off

Inequality can affect the rate of growth through two mechanisms: the socio-political and the economic (Ros, 2000). The first mechanism (the socio-political one) is linked to the "distributive conflict". Inequality tends to generate social and political pressures concerned with the redistribution of incomes through fiscal policy.

232 Our findings are very similar to those obtained by Litchfield (2002), who argues, analysing years 1990–2000, that if the highest income decile is removed, then the distribution of income in Chile would not be too different from that of European countries.

233 Through its employment survey, the University of Chile provides the only homogeneous source of information on the distribution of income in the long term. This is annual data on revenue for a rotating sample of households in Greater Santiago, whose consistency is provided by the use of a questionnaire and measurement methodology that has remained essentially unchanged since 1958.

Moreover, the neoliberal side argues that fiscal policy has negative effects because higher taxes and public expenditure can reduce the rate of investment and therefore growth. However, these worries are mostly ideological. Neoliberals do not evaluate as positive effects of public spending in the social area, neither any other area in which public policies be oriented to improve income´s distribution. In their view, a better income distribution only must be inducted by a progressive improvement in remunerations, as a result of a good performance of firms and labour markets, derived of trade openness and liberalization.

In our opinion, there is no doubt that, in the long run, an improvement of the primary sources of income based on the relative productivity of the factors of production, would be an optimal path. But this do not mean that the current distribution of income should be maintained which if it were optimal and that any changes to it should be considered sub-optimal. Also, should be acceptable the social policy be aimed to manage the impact of the opening of the poorest sectors of the population which, markets 'shortcomings do not allow addressing immediately. However, assimilate the progressive distribution of income with an eventual influence of trade openness on firm's productivity, only would be reasonable in a perfect competition economy, with full mobility of factors and without frictions in the process of resources reallocation. As well, as we have analysed so far, that does not seem to be the case of Chile.

There many authors who do not agree with the neoliberal point of view about income re-distribution but emphasizing additional points applicable to the short-term distributional policies. According to Alesina and Perotti (1994), a reduction in inequality through fiscal redistribution in favour of the most vulnerable sectors, can improve the rate of economic growth, because incomes may be transferred from rich to poor by relaxing restrictions on their investments, so that the most vulnerable person can invest in human capital. In addition, economic growth can rise because fiscal redistribution may relieve socio-political pressures towards higher taxes on the rich, and thus promote economic efficiency and growth in the long term, based on certainty and stability.

Another line of criticism of the neoliberal vision questions the presence of a reverse relationship between equality and growth (the "economic trade-off"). This is a long-standing debate. Almost thirty years ago, Lindert and Williamson (1985) stated that American and British history suggests that the growth-equality trade-off should be redirected towards a more fundamental debate on the efficiency and equality trade-

off, quite assuming that growth is a by-product of economic efficiency. Based on that approach, they asses that any relevant income distribution, rather than generate inefficiencies and fall of GDP, will induce improving in efficiency and growth.

From another perspective, some non-neoliberal authors like Acemoglu (1996), also defy neoliberal point arguing that an economy that is based on low levels of inequality will show a clear downward trend in this area and will not reach a balanced growth. On the contrary, an economy that assumes as a core task reduction of the high levels of inequality, will reach a higher growth level.

The temporal evolution of the Chile´s economy looks like confirmation these last points of view, because it is clear that Chilean GDP growth is not positively correlated with the presence of progressive income distribution. This is one of the crucial challenges of the economy in the area of equality, and the current likelihood of achieving this target, need to be, point by point, carefully analysed, such which we will try to do in the following subchapters.

6.13. Inequality and GDP Growth

Chile is often described as a country incorporated into global economics in a solid and diversified way. This assertion has become a reality during the period of 1990-2009, through the subscription of free trade agreements with countries whose markets together correspond to more than two-thirds of the global population (Direcon, 2008). This represents a significant success for a country with a relatively small internal market. Openness has consolidated an export-led development strategy associated with higher rates of growth and poverty reduction. However, this process is less solid than it appears, especially considering the previously stated observation that Chilean exports are mostly commodities that do not support the process of creative destruction and technical progress diffusion.

If we disaggregate Chilean economy sectorial or by size of firms, it presents very weak productive linkages and high levels of economic concentration conversely, the process of poverty reduction is weak and highly dependent on the permanent presence of high growth rates that are very difficult to sustain without technical progress complemented with high and increasing social public spending. Thus, in Chile there is a growing perception that the country is currently experiencing an extremely fragile development

process[234] with a feeble economy and with poverty and inequality levels incompatible with the status of a developed country (Tokman, 2004; Lamarca, 2009; OECD 2011b). As we can see in Figure 6.16 next, whilst GDP grew three times its starting size, the employed labour force only grew to the extent the population became economically active. Furthermore, the sector of the labour force that is unemployed grew much more, despite fluctuations, above the growth of the economically active population. This means that the Chilean economy has not been able to improve levels of employment in any significant way. We estimate that problems of inequality are not only originated in labour market, as we will demonstrate later, productive arrangements within chains and sectors explain an important part of economic concentration.

Specific performance of labour market is highly determined by that process and, in any case, reduction of unemployment and under-employment must be a basic condition for a sustainable reduction of inequality. Nevertheless, the average rate of urban unemployment in Chile during the period 1990-2009, was 7.9%, a level not radically different to the Latin American urban unemployment average rate of 8.9% (ILO, 2011), meaning that, labour market performance, even in condition of high economic growth, clearly is not collaborating so much to improve equality and progressive income distribution.

234 As pointed out by ECLAC (2011), people have internalised the idea that material aspirations are satisfied by well-paid, stable and protected jobs. According to this logic, those persons who are unemployed, or in sporadic employment, face barriers to social integration and the affirmation of their identities and self-esteem (Kaztman, 2010), generating a gap between aspirations and expectations and resulting in reduced subjective well-being" ECLAC (2007a).

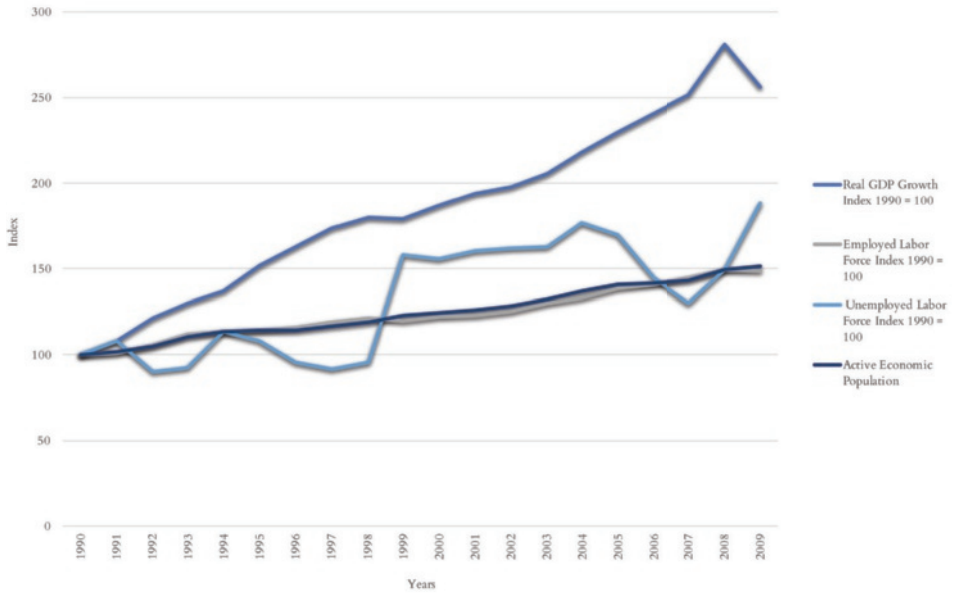

Figure 6.16. Chile 1990-2009. Employment, Unemployment and GDP Growth
Source: Author´s elaboration based on data from INE and BCCH (1990-2010).

As figure 6.16 display, while GDP has grown two and a half times, the employed labour force only has grown by the same measure as the economically active population. Furthermore, the fraction of the labour force that is unemployed has grown much more, standing -despite its fluctuations- above the growth of the economically active population. This means that the Chilean economy has not been able to significantly improve levels of employment, a necessary (but not exclusive) condition for a sustainable reduction of inequality. This reality contradicts the widely-held belief of the same centre-left sector who declare that post-dictatorship Chilean governments would implement a new development model by committing to work very focused on easing frictional unemployment, and hence become more egalitarian, inclusive, and different from the neoliberal one.

Despite these optimistic expectations about post-dictatorship economy´s perspectives, as we have shown in several previously analysed areas, the dynamic has not proven to be as positive as IMF and local and non-local neoliberal expected (Stiglitz, 2003). Moreover, it is pending define if the presence of structural unemployment and underemployment and productive inefficiency are alike variables that determine the Chilean economy's difficulties to improve their equity levels or, on the contrary, only one of these factors is the determinant of inequality and the other one a derivative.

This dilemma is not new to the discussions about the Chilean economy. From the standpoint of the ECLAC, authors like Fajnzylber (1989) had sustained that the radical openness of the internal market in Chile would produce the rationalisation of an extractive model, which he denominated as "rents-seeking system". His main argument was: If the early distribution of power remains unchanged and concentrated, independently of declared intentions of trade openness, the consequence would be an industrial falling off and an integration of the national economies within natural resources-based global markets, followed by an over-development of trade activities and others linked to financial intermediation (op. cit., 1989: 62). Within this framework, inequality in income distribution would be the ultimate expression of the action of three sources of inequality: 1) the unequal property of capital. 2) Low labour incomes in relation to the remuneration of capital and 3) the unequal productivity of the different segments of firms, which is usually referred to as structural heterogeneity.

The position of post-dictatorship Governments in relation to the feasibility of openness and liberalisation inducing changes to those sources of inequality has been, without a doubt, far too optimistic and based on neoliberal assumptions. In official speeches, some former Chilean economic ministers (Foxley, 1993, Velasco and Tokman, 1993) have argued that a strategy of openness and market liberalisation as followed by Chile would be optimal. They refuse arguments like the exposed by Fajnzylber, assuming that even an abrupt and sudden expansion of market competition would be optimal, reducing structural heterogeneity, determining the salaries according to labour productivity, redistributing the investment in human capital, providing the best way improve equality from labour markets, in a way slowly but permanent.

Challenging that approach, from the first decade of this century, it become clear that the trade openness process would have serious difficulties introducing competition in the Chilean markets that, up to that point, were anything but competitive (TDLC, 2011). On the other hand, was clear that the quality and distribution of human capital in Chile continued to be insufficient (Brunner and Elacqua, 2003) and educational reform programs promoted by the new administrations, were beginning to look like a "never-ending history". However, the optimistic view of post-dictatorship elite was not affected by that evidence, despite the undeniable presence of an issue which was impacting additional incomes distribution: "structural heterogeneity". This issue deserves a split up and detailed analysis, given that heterogeneity among different segments of Chilean productive fabric is very acute and their impacts on labour market and income distribution have great dimensions.

6.14. Structural Heterogeneity and Institutional Arrangements

Productive heterogeneity problems are related to market interactions between different sectors and sizes of companies. If large companies increase their market share due to increased productivity, in addition to their others competitive advantages, following the neoliberal thinking, this process must be assimilated to current economic development.

Given the pressure exerted by that process, the decline of small businesses, neoliberal said, should be seen as a natural and positive phenomenon (Cabrera et al., 1999, Fuentes et al., 2006), which would multiply the number of workers (especially those of higher productivity) that move from small firms to large companies in search of higher wages. However, as we have formerly analysed, there a lot of evidence about the fact that when Chilean large enterprises increase their market share, their wages do not move in the same direction, (Ferrada and Reinecke, 2004; CASEN 1990-2009; INE, 2006-2009).

The expansion of the GDP of the Chilean economy is mainly based on the growth of product and sales in the larger enterprises. For this reason, our first interest is to enquire as to whether this increase has been translated into higher wages, or if the evolution of wages is in harmony with the evolution of productivity of each size of firm. If we focus our attention on the behaviour of the labour market disaggregated by company size, the available information about wage structures reported in national surveys (INE, 2010) confirms our former assertion, productivity and wages evolution diverge. Nevertheless, although the highest levels of productivity are concentrated in large Chilean companies, their wages likewise are not correlated positively with it; small businesses have a much more progressive salary structure than the large companies despite their relatively low productivity.

Labour incomes consist principally of wages, whose level varies considerably amongst the different sizes of companies (Mizala y Romaguera, 1993). The Average Wages and Labour Costs Survey of INE (2010), shows that in December 2009 the average salary of people employed in large companies reached CH$ 433.317 (around US$865) per month. On the other hand, the average wage paid in middle-sized companies amounted to CH$ 332.730 (around US$664), and in small companies to around 325.261 (US$586). That means that, on average, there is a 25% difference between wages in larger and small firms, yet these percentages are not correlated to the differences in productivity existing between the different sizes of companies.

If we analyse the aggregate behaviour of wages in the Chilean economy it is clear that from 1994 onwards, the evolution of average real salaries moves below the increases in average labour productivity. This demonstrates a trajectory of growing separation between the evolutions of both variables. However, if we disaggregate figures by firm size, the situation is different. In Figure 6.17, it is possible to observe that in 2006, the absolute wage value of large firms was around 24% higher than the wage value of medium and small firms. Fours year later, in the last month of our period of analysis (December 2009), small companies maintained a similarly large differential of wages compared to large companies, but the middle-sized companies had reduced the differential to just 20%.

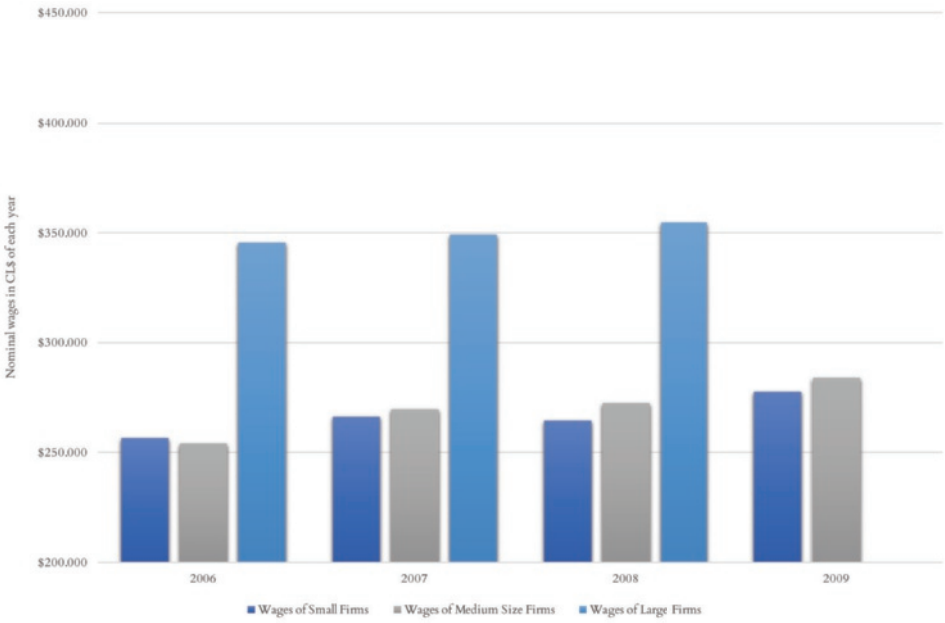

Figure 6.17. Average Wages by Size of Firms. Chile: 2006-2009
Source. Author´s elaboration based on data of INE; all sectors and economic activities.

The Chilean Ministry of Economic Affairs (Minecon, 2015) assumes that on average, the labour productivity of large companies is 4.8 times that of small ones and 4.1 times that of medium-size firms. On the other hand, our own estimations based on data from IRS (2010) show that in 2006, small firms had average sales by worker's equivalent to 16.3% of similar sales in large firms, and in 2009 of 16.6%. Middle-sized firms that in 2006 had average sales by worker of 21.3% in 2009, present only 20.5% of average

sales in larger enterprises. It is clear that there is a tendency for large firms' wages to evolve in a way that is highly dissociated from labour productivity, a trend that is not observed in small and medium enterprises.

From Figure 6.17.[235] it is possible to observe that Chilean wages are not only very low, but also the wage´s value of large companies and of small and medium firms are not too different, fluctuating around 200 US$ per month per worker throughout the period analysed. In effect, the difference between the value of average sales of large companies in relation to the small and middle-sized companies ranges between US$12000 and US$13000 per worker (SII, 2010). This process has happened to such an extent that large Chilean companies have achieved growing market power, starting to manage the wage levels of the entire economy.

The remunerations paid by them are very close to the average wages of companies of lower productivity. This situation clearly demonstrates the capacity of larger enterprises to build institutional arrangements that define the Chilean wage structure as a whole. This market power allows them to appropriate, under the form of "capital rents", the on-going differentials between enterprise productivity and wages paid by them.

In summary, the existing wages differentials between different sizes of companies are not correlated to differences in productivity between the various sizes of companies which belong to different Chilean productive sectors. Besides the fact that the Chilean model is clearly not contributing to equity, it is not at all clear whether it is contributing to economic efficiency. However, it is clear that it is generating oversize capital rents in large enterprises. Independently of the estimation´s way of capital remuneration, conceptually speaking, it is not a residual.

Capital rents are determined by the level of the marginal productivity of capital, and, on the other side, the wage of workers is determined in a similar way by the marginal productivity of labour. Therefore, according to neoclassical economics, if a productive factor is not reattributed according to the marginal productivity, the inevitable result will be the misallocation of resources that will result in economic inefficiency. Given that, we can conclude that low levels of equality (and their effects on income distribution, poverty and employment) are closely related to the way in which market

235 Income´s data are reported here from starting in 2006, since the nominal series of real wages of the INE, from 1990 to 2006, are not disaggregated by size and may not be spliced with the data of the new series.

power affect labour markets and their LSE business relationships with small firms. This situation, in turn, is strongly connected to general economic concentration prevalent in Chilean markets as a whole.

Like has been displayed in Chapter III, LSE define their wages managing their market power and increasing their labour demand in order to homologate their remunerations to the MSME wage levels, dissociating this small spread existent between sizes of enterprises from productivity enhancements induced by labour reallocation from MSME to large enterprises.

The main mechanisms that allow that situation are related to institutional arrangements, expressed in labour laws, inherited from the dictatorship. These practically inhibit the formation of trade unions, or subtract from them any bargaining power and negotiation effectiveness. Multiple other arrangements consolidate these institutional devices: The modalities of operation of labour courts and their high costs; the possibilities of administratively split the companies to prevent the quorum necessary for the conformation of trade unions; the mechanisms of workers on strike´s replacement; the precariousness of the labour protection of union´s leaders, etc., are just a few of the many elements that make part of the institutions of governance that regimented the Chilean labour markets.

On the other hand, on the side of the business relations between companies of different sizes: the reduction of State resources for training of small businesses workers, the prohibition of establishing mechanisms for financing mandatory and automatic for the operation of the MSME entrepreneur´s associations, the many regulations and taxes that erode the profits of the MSME limiting its options to improve labour remuneration; the rules governing interest rates to be charged by banks to the MSME. There exist multiple other arrangements that make up a solid institutional fabric, which is expressed in a specific kind of labour markets operation that concentrates the low remunerations in the MSME and reduces artificially wages' pressures on large companies. Naturally, that kind of arrangements is very helpful to LSE in its process of economic rents production and on the concentration of these in few hands. That situation allows large enterprises to exert its market power in labour markets by mean of a process whereby they use the low productivity levels of small firms as a "wage-roof" that lets them maintain institutionally depressed wages.

This mechanism allows them to obtain large amounts of economic rents based on the capture of the market value of productivity differentials existing among different sizes of enterprises. However, if contrary to neoliberal assumptions, flexibility and low bargaining labour power did not produce a system of "labour-efficiency prices", it is highly possible that the actual labour market operation, on the one hand it will decrease the productivity of the workers to whom wages are reduced. On the other hand, they will allow the presence of economic rents highly dissociated from those mechanisms than make possible an efficient resource allocation that would foster productivity. Subsequently, if the operation of the labour market, induced by their mechanisms of governance, acts against productivity, it constitutes an issue that will limit the maintenance of the high rates of growth, which characterised the golden age of the Chilean economy.

Why then did the new authorities not act to correct this situation by fostering "market competition-based" mechanisms, or acting to prevent growing market powers of LSE? Why, on the contrary, support maintenance of the institutional arrangements which, from the production side and from the labour markets, maintained the neoliberal status quo?

Given the unstable context existing during the first years after the dictatorship ended, the path adopted by the new Chilean authorities included, for political reasons, the decision of not to alter the big economic rules of the game and the institutional arrangements that kept labour remunerations institutionally depressed. After some time, when the political context had become friendlier to the establishment of more inclusive labour institutions, the neoliberal rules of the game had become the "normal operating arrangements" (on labour markets and on productive chains) and willpower to introduce institutional changes had actually disappeared.

At that time, it was increasingly difficult to change the national save-investment process. This was already based on the presence of high amount of capital profits, made possible by the permanence of arrangements that define wages and business relationships widely used by large enterprises, based on their growing market power applied over the labour markets and over MSME. After that the arguments against changes start to be claimed, by right and left-wing economists, basing on the negative effect on investments that any alteration of the institutions associated to the development model may produce.

6.15. The Post Dictatorship Policies of Social Spending as a Tool of Income Re-distribution

The relationship between poverty, inequality and economic growth existing in Chile, clearly shows that growth is not a "silver bullet" that fixes all problems. The Chilean supporters of the neoliberal model have argued that, to the extent that it promotes the growth of the Chilean economy, the poor should have benefited. Therefore, to the extent that the trade openness and market liberalisation drive GDP growth, this situation should have been translated into a decrease in poverty and an improvement in the distribution of income associated with the increase in the productivity of labour. Throughout this chapter, we have shown that none of these projections has become reality.

Although during the period 1990-2009, Chile experienced, as an average, a substantial reduction in headcount poverty and a slight and irregular reduction in inequality, the evidence reported here shows a worsened of these trends after the Asian crisis 1996-1998. Whilst between 1998 and 2003, the absolute number of poor´s household decrease, after Asian crisis an increasing number of Chilean households, already classified as non-poor, fall down above the poverty line. The same situation happens after 2006, but in a worse situation, given that in that second period the absolute number of households below the poverty line increased against the grain of the pace of growth´s rate of GDP.

On the other hand, the evidence reviewed here shows that economic growth has played an important role in poverty reduction. Nevertheless, there is no evidence of a similar effect on inequality, a situation that is clear when observing the low correlation between the GINI coefficient and the growth of GDP per capita.

The macroeconomic policies developed by authorities have not been contributing to the enforcement of a pro-equality and pro-poor evolution. When the economic authority decided to adjust the aggregate spending of the economy during the Asian crisis, it decided that the cost of the crisis should fall on the MSME. This option resulted in an important segment of employment moving from small enterprises to large ones. Whilst in 1990, 54% of formal employment was produced by the MSME in 2009 they only produced 47% of this employment.

However, this displacement of labour was not associated with increases in productivity or with increases in wages. The different estimates of TFP previously reviewed and the official salary statistics (INE, 1997-2009) for that period, show that productivity began an irreversible tendency to decline and stagnation, while wages clearly did not adjust to productivity of the new companies, but they remained at levels very similar to those that the workers had in their old jobs.

The distribution of income has not been seriously encouraged by the kind of resource reallocation process induced by trade liberalisation. After a "golden period" (1985-1998) with a rising rate of growth, the Chilean economy has evolved steadily downward.

Given the elasticity and semi-elasticity of poverty reported here, a path of poverty reduction seems possible only in a scenario similar to the golden period. In that period, the GDP exhibit an average growth rate of 7.3% per year, producing a poverty reduction of 23 percentage points. On the other hand, also it seems clear that, in periods of high growth and low growth, the distribution of income did not show major tendencies of improvement. It is our opinion that the institutional arrangements that characterize the Chilean markets are the variable that conditions the current regressive income distribution. Without creating a change on those economic institutions, it is hard to imagine that trade openness and liberalisation could generate processes in which resources allocation would be optimized, enhancing the productivity and competitiveness of the Chilean economy. The absence of such kind of dynamic is the reason why Chilean economy is relatively impervious to the processes of economic openness and liberalisation.

It is clear then that redistributive policies based on CTP, must be complemented by policies that are very different to the neoliberal ones and not limited to marginal tax changes or, worse, to waiting for the "trickle-down process" to resolve problems. The Chilean experience shows that contrary to neoliberal assumptions, without modifying primary incomes (trough installation of genuine competition on markets, an improving in compensations and a progressive tax system); it is difficult that benefits of openness and growth be transferred to the poor. In countries such as Chile, in which income is highly concentrated, such redistribution process focused on primary sources of income, would have a significant effect on the fight against poverty and in sustaining an aggregate demand that would foster productive development and a process with a more progressive distribution of economic growth.

6.16. Conclusions

The evidence reported in this chapter allows us to conclude that:

- From the point of view of the structural sources of the growth, trade openness has deepened the extractive regime dependent on international prices of raw materials. Obviously, in the best part of the price´s cycle, the growth´s rate of international demand for those commodities impulses the economy, but when prices fall, it produces a serious external shock. In this context, the transfer of incomes through rising consumption levels has showed been a highly ineffective way to produce a better income distribution and to reduce poverty in a significant and sustainable way. However, the intention of post-dictatorship governments of uses a second device and reduces inequality by means of monetary transfers, does not create stable bases for a more egalitarian society, or a solid foundation for growth. The growth of GDP maintained, during some time, very good rates, but when the high price of raw materials ran out, the brisk growth of the economy also stopped.
- The Chilean process of economic growth has not been able to reduce poverty in the way that was promised by the supporters of Chilean model. On the contrary, the Chilean economy is showing over time, less and less capacity to produce major reductions in poverty through economic growth. The estimations of elasticities of poverty displayed here, allow us to assess that growth exerts a moderate-to-low level of incidence on the poverty reduction. These elasticities have been decreasing over time, and the economy has even produced reversals in the sign of the aforementioned elasticity. Contrary to the neoliberal hypothesis, economic growth reduces in a relevant way poverty headcount only when GDP displays high growth rates, such as those that placed Chile amongst the five countries with the top growth rates in the world, but poverty is not reduced if those rates are not present. If in the next half-century, Chile hardly achieve similar rates; further poverty eradication will become an implausible goal.
- During 1990 to 2009, Chile failed to improve its unequal distribution of incomes and the Chilean Economy the regressive situation inherited from the dictatorship hardly varied at all. Despite the acceleration of economic growth and the deepening of the radical trade openness of the Chilean economy, during the analysed period, income inequality remains high and stable. The results of this research tend to confirm the relative constancy of such inequality

in Chile, during the twenty years analysed, whether measured by the Gini Coefficient, Kakwani and Reymond-Smolensky indexes, or as proportions of the highest incomes deciles (and those that follow) and the poorest.

- Long-term income distribution data show that the Chilean economy has high levels of inequality that persist over time, and in turn, reflect the effect of long-standing structural factors accelerated by the implementation of the neoliberal model. Throughout the process of trade openness deepened during the period 1990-2009, the widespread use of market mechanisms in the allocation of resources, following the reduction of the participation of the state in economic activities, has failed in their aspirations of total poverty eradication.
- For the period 1990-2009 that we have analysed, available nationwide data indicates that at the beginning of the period inequality dropped, but this trend was quickly reversed so that its period ends with inequality levels similar to those at the beginning. It is a paradoxical result, since the strategy of the post-dictatorship governments, inaugurated in the 1990s, was to reconcile economic growth with higher degrees of equity.
- Monetary subsidies do not seem to exert a major impact, because in Chile the main distributive inequality is linked to non-labour monetary incomes, which are much more concentrated in Chile than in other countries in the region and, in the remaining countries of the OECD. Our study shows that inequality in Chilean society is largely explained by the impact of the concentration of such incomes in the first quintile
- Additionally, there a lot of evidence that Chilean economy shows a strong concentration in the ownership of productive assets. At the same time, it shows a significant gap between productivity growth and the increase of wages, and among wages paid by different size of firms. MSME pay wages closely related to their productivity, and large firms pay wages that are highly divorced from it. The presence of a neoliberal institutional environment goes along to extremely asymmetric institutional arrangements, both in the labour markets and on business relationships between small and large companies within productive chains and economic sectors, seem to be at the root of this process of concentration. However, this issue will be meticulously analysed in the next chapter.
- The analysis reported in this chapter allows us to conclude that there are powerful institutional factors that explain why Chilean markets dynamic are unable to reduce poverty and produce sustainable economic growth. That is the reason why Chilean markets presents a low growth elasticity of poverty, which

makes it increasingly difficult to overcome poverty through mere economic growth. Deep institutional asymmetries in the labour markets tend to generate a strategy of cheap labour, matching wages in large industries to wages in MSME of low productivity. That spread is allowing LSE to widen the existing differential between productivity and wages in the Chilean labour markets. Similar institutional arrangements are applied to the relation between different sizes of enterprises. The outcome of that process has been a profits transference from MSME to LSE reflected in decreasing market shares of smaller firms.

- During the analysed period, the radical trade openness of the Chilean economy, has deepened its original extractive dynamic instead of focus on productivity. Given that the declared purpose of the post-dictatorship authorities was to introduce some degrees of equality into the process of economic growth and that aim appears very demanding, their discourse began to dissolve in the grey area of compensatory social policies. Seeking to reverse the social effects of regressive income distribution with cash transfers (quite limited otherwise), was not a successful path. However, if the policies that succeeded the dictatorship would had focused on modifications of the institutional environment and institutions of economic governance, the result could have been different.
- It has become extremely difficult for the Chilean economy to improve its progressive income distribution based on primary sources of income, given distortions existing in the operation of domestic markets. The wide battery of subsidies to the poor, have failed. They tried to complement the secondary sources of income generation in order to make it possible to poor families overcome the poverty line, however poverty is actually linked to the weak poor's primary sources of incomes and any secondary improvements has been able to change this situation. The quantitative indicators estimated here, and they measure the process, show that, despite the reduction of headcount poverty and the improvement in the incomes of the poor, the social expenditure of the Chilean State between 1990 and 2009, has nod exerted a meaningful progressive character.
- In sum, we can conclude from evidence reported in this chapter, that the neoliberal hypothesis which declared that, without intervention of other agents than free markets, the Chilean model would produce a decrease in poverty and incomes inequality, can be considered falsified. The application in Chile of the neoliberal model, has only led to the reduction of the headcount poverty given State´s intervention by means of CTP. Moreover, it has done so in a highly-conditioned manner due to the presence of a poverty line whose absolute

value has remained almost unaltered (in real terms), throughout 20 years. This has happened despite significant changes observables in the composition and valuation of the basket of goods to which said line is associated. Similarly, those persons or families who overcome this line, according to the Casen surveys (1990–2009), do not do so in a permanent or stable way, going in and out with high frequency, moving from the ranks of poverty and coming back to it very easily.

- Given this fact, in the following chapters, we will try to show in a deeper way what are the institutional variables which condition the Chilean distributional and allocation issues, and why they are weakly inaccurately influenced by economic openness and changes in the new system of relative prices that it has produced.

Chapter 7

The Effect of Institutional Arrangements on Economic Concentration

In previous chapters, we have shown how the Chilean economy has been generating extreme economic concentration and intensification of its structural heterogeneity. We have also shown how, despite the orthodoxy of the Chilean economic policies, a convergence between its GDP and productivity with more advanced economies is only a diffuse trend, whose goals will be extremely difficult to accomplish. In the same way, we have made evident that the process of headcount poverty reduction exhibits tendencies that are not sustainable and that the reduction of inequality is a virtually absent phenomenon. Given these findings already reported, at this point of our analysis, we will try to understand how the Chilean productive fabric is organised, focusing our attention on the areas that seem crucial to explain the specific characteristic of neoliberal institutional arrangements that shape the governance system prevailing in the Chilean markets.

The objective of this chapter is to report our process of exploration of economic relationships and institutional arrangements existent between companies of different size and productivity strata. Here we specifically analyse the current economic relationships among large, small and medium enterprises, understanding them as outcomes of the institutional arrangements established between the different productive strata of the Chilean economy.

In the first place, we proceed to find out what are the specific linkages and economic exchanges created between the aforementioned business strata throughout the implementation of the neoliberal model of development and then we analyse what are the specific institutional arrangements that have shaped them. From there, our analysis is focused on defining the relationship between both elements and on the impacts that the trade openness and market´s liberalisation of Chilean economy have had on these. Finally, the findings of this area of research will be used in order to evaluate the respective role of the relative price system and of the institutional arrangements that have given their specific form to the neoliberal development model that has been consolidated in Chile during our period of analysis.

It is with that in mind that we built a disaggregated version of the Chile´s Input-output Matrix 2008 (IOM 2008). That Matrix was constructed to establish the effects of arrangements present, in the areas of production and consumption, among the three levels of size and productivity of firms existing in the Chilean economy. The final and intermediate demand, as well as the intermediate consumption, has been disaggregated into three strata of companies possessing three productivity levels (low, middle, and high) for each one of the nine main sectors of economic activities. Those levels of productivity were associated with three sizes of enterprises; low level of the productivity within micro and small enterprises, middle productivity within middle-sized firms, and high productivity within large enterprises. In this matrix, the value added was also disaggregated into the same three strata or sectors. The final demand included a registry of the government consumption and of their interactions with the differently sized firms, while the consumption of goods and national services by households, was also disaggregated into three layers defined according to its per capita income level: high, middle and low.

Using this methodology, we obtained an abstracted matrix for the year 2008, which we will call the Structural Economic Matrix of the Chilean Economy (SEM). The SEM allowed us to register sectorial cross-relations and to quantify the impact that institutional arrangements induce over each productivity and size stratum exerts over the structure of the Chilean economy, and vice versa.

7.1. The Institutional Arrangements in Chilean Markets

This research has assumed the view that, given that institutions are mechanisms of governance, explanations about their operation should be organised around the partial analysis of these mechanisms, rather than on the development of general theories (Elster; 1994:75). Within this framework, analysis of the operation of markets, as well as specific forms that assume the institutional arrangements that determine the resource allocation between firms and markets in the economy, has been present in all our analysis.

In this chapter, we understand governance structures to be the institutional matrix within which the integrity of a relationship, or a related set of transactions, is carried out. Therefore, this chapter is focused on the following areas:

1. Analysis and dimensioning measurement of the set of transactions carried out in the Chilean economy.
2. Description of the main features of the structure of institutional arrangements, established by the Chilean neoliberal model, which govern those transactions.
3. Analysis of the alignment or non-alignment of institutional arrangements around transaction cost minimisation purpose.

7.2. The Business Model as Crystallization of the Institutional Arrangements

In the Chilean case, growth processes based on the export of natural resources and a strong attraction of foreign direct investment, according to neoliberal-neoclassical forecasts, should have been producing multiple economic linkages that enhance and increase productivity across the productive fabric. However, if there were severe limitations to the distribution of economic gains beyond the select business groups that control economic and political institutions, this hypothesis should be considered falsified.

We understand, following to O.E. Williamson hypothesis (1996), that Market institutions create and legitimate norms thought the interaction of relatively autonomous economic actors, typically without long run commitments to each other. Evidently the norms and conventions of the markets are related to the matter of prices, but without a well-defined institutional frame, there is not a single and clear quantitative expression of such prices, nor a convention to which actors can use them in order to proceed to a more efficient resource allocation. For that reason, we have emphasised here a singular point of view: In the area of the business relationships, governance institutions are a coherent set of arrangements which tend to be expressed through the features exhibited by the "business models" that dominate the economy.

That approach has been used in this chapter as a tool to understand how the institutional arrangements of the Chilean economy as a whole are organised and what the specific arrangements prevailing in their different sectorial markets are.

In the literature, the interest in analysing business models has been growing since the beginning of this century (Chesbrough and Rosenbloom (2002); Magretta J. (2002), Baden-Fuller and Morgan (2010); Zott et al (2011); Arend (2013); Baden-Fuller and

Mangematin (2013); Roome and Louche (2016)). Business models are generally seen as the pattern from where businesses take shape. They essentially are a comprehensive set of institutional arrangements present in the areas of regulation, strategies and business practices. The analysis of these models allows us to form a description of the ways in which businesses take over the maximum value of the products or services, which they have created or contributed to create (Lai et al 2006).

The conceptualisation of business models has been increasingly oriented towards the understanding that they are integrating a wide combination of performances and strategic alternatives adopted by the companies, linked to the central logic of the creation and capture of value within a network. This understands the logic of the companies, essentially, as a process of organisation and capture of value operated through business models.

Here we will try to demonstrate that the previously reported findings of our case research, and the conclusions extracted from the data analysed in this chapter, support the view that relations between sizes of companies are essentially determined by the business model within which each company decides (or is compelled) to operate. We will show that when we aggregate the particular insertions of different companies and segments of companies, it is possible to define the kind of business model that has become predominant in the economy.

From this perspective, relations between companies of different sizes will be analysed in this chapter from two different aspects:

1. The first is focused on an area that is a central part of the business models in which is engaged each company: The sectorial distribution of final and intermediate demand which, given the specificity of each market and its assets, are, essential parts of each business model. The insertion of each firm in specific sectorial niches granted by a singular level of profits, will be here defined in terms of these two variables of demand distribution which define the sectorial distribution of value added, an area that define which firms have the possibility of became winners and those who have no chance of improving their situation.
2. The second is focused on another area of the demand side, complementary to the previous one: The size distribution of final and intermediate demand between different sizes of companies. These specific arrangements consolidated in a business model, let that large corporations define market share of each

one of the major business segments (LSE and MSME), within the markets that they govern. This distribution of production, inputs utilisation and final utilisation (consumption) will also define the mechanisms through which it will be possible to achieve the defence or expansion of the market share of each size of companies.

The combination of both aspects has defined features of the business model governing the Chilean economy as a whole and hence the institutions of governance that prevail.

In those industries that operate in a context of real competition and without major asset specificities, the companies face given-prices provided by markets in which they have free entry and exit to. In these markets, firms can attempt strategies of innovation and differentiation of their product or services in relation to its competitors, but those will only have short-term effects. It is very difficult to project a singular business model like that, far beyond the limits imposed by competition in which innovation and differentiation tend to produce only transitory effects.

In fact, in markets with a high level of competition, business models are exogenous to the company, in the same way as the prices that it faces are. Then, the greater a market's competitiveness and the fewer its asset specificities, the more exogenous the adopted business model will be.

Reciprocally, at a lower level of competition and higher asset specificities (natural or built), endogenous factors have a greater weight in terms of the implementation of some specific business model oriented to the success of firms by means of tools that allow them, in the words of Aghion (2005) to "escape from competence".

The feasibility of placing in function a specific business model is not only a function of the strategic capabilities of company's managers. It is also a consequence of the endogenous or exogenous character of the institutional arrangements that enable, make difficult, or render categorically impossible, the legitimacy of a particular business model.

7.3. The Economic Concentration as a Sticking Point to Innovation

The levels of competitiveness prevailing in the markets and the sectorial asset specificities are a crucial variable which influences the business models that will prevail in each market in a decisive but not unique way. If a company innovates, generating products or differentiated services, or simply making an operation more efficient, it is thereby building its specific way towards greater control of their markets in which it is acting. However, it will be the same strength of competition, which will make things return, over time, to the original competitive situation, to the extent that innovation and efficiency are absorbed by the markets and become available for all other firms.

However, the most recent information available in the Fourth Longitudinal Survey of Companies on Research and Development in Chilean Companies (Minecon 2017) show that the dynamics of innovation processes are far removed from the competition context described above.

Only 12.1% of companies in Chile declare R + D, that is, nine out of ten companies do not (87.9%). The percentage of large companies that declare R + D within their stratum (28.6%) is three times greater than that of micro companies (9.6%), a little more than twice that of small companies (12, 1%) and one and a half times that of the medians (20.7%). The four economic sectors that, on average, perform the most R & D are: Information and Communications (36.6%), Electricity, gas and water supplies (23.6%), Financial and insurance activities (20.7%) and Professional, scientific and technical activities (20.5%), that means that are non-tradable specialized sectors. The four economic sectors that on average perform less R & D are: retail and wholesale trade (10.8%), artistic, entertainment and recreational activities (8.9%), agriculture, livestock, forestry and fishing (6.7%) and Transport and storage (3.7%). Approximately one quarter of the companies in Chile (26.1%) state that they carry out R & D without the appropriate facilities and without the necessary qualified personnel. Almost half (43.1%) do so with facilities or qualified personnel, but not both, and close to one third (30.8%) do so with facilities and qualified personnel. Moreover, among the small number of companies that do R & D in Chile, facilities and qualified personnel (27.3%), only 25% of them consider that their products are very sophisticated, while only one in ten companies do not. do R & D (10.8%) says achieve such a level of sophistication. Approximately one third of the companies that do R & D with facilities and qualified personnel (31.7%) consider that their products are very modern, while

only one in ten companies that do not do R & D (10.4%) says to achieve such a level of modernity (Minecon, op.cit).

All the above shows that the R & D carried out is of low quality and therefore the explanations that try to explain the Chilean phenomena of concentration extrapolating explanatory models explainable to USA, Korea or Israel, are not sound.

The most recent figures available in Chile show that the dynamics of innovation processes are far removed from the context described above. On the contrary, when there is permissive regulation about what is legally possible in the field of business or if there are the possibilities for firms to influence the definition of new rules of the game, the result will be like the formerly described lack of innovation. We will see how the virtuous mix innovation-differentiation-efficiency; won't be the variable that will generate the success of larger firms. Instead, the leading role will come to be played by the firm´s actions on the rules and regulations that may inhibit or permit the continued growth of their participation in the markets.

7.4. The outcomes of neoliberal institutional arrangements

The consequences of that situation may be clearly visualized using the Input-Output Matrix of the Chilean economy, which reflects the origin and destination of transactions or cross-sectorial economic flows, depending on the levels of domestic production of each sector of activity, adding imported of goods. When the interrelationships of the matrix are disaggregated by enterprise size, we additionally access to similar information on each size of company operating in every sector of the economy, Then, the Chilean economy analysis that we will develop onwards by means of an IOM approach, will provide us with abundant information that will allow us to characterise the predominant business model in the Chilean economy. It will be presented as an articulation of certain institutional arrangements which have crystallised into business practices that, in some respects have been internalized by the agents and in others is the source of the conflict between them. We postulate that these arrangements that define inclusion or exclusion of firms in trade openness gains are an indissoluble part of the neoliberal development model implemented in Chile and explain the hard boundaries confronted in the country by a project of sustainable development economic

By means of that analysis, we will show how the trade openness and market liberalisation have not dissolved the market power of big Chilean companies. To the contrary, it has brought an inverse effect, to the point that the bulk of intermediate and final demand in the economy has fallen under the control of a handful of large market power firms.

The market power of big Chilean companies has been forged alongside the installation of the neoliberal model. At the level of the main rules of the game that define the institutional environment, this power was achieved through the political participation of large corporations in the installation of a dictatorial government that laid the foundations of the neoliberal model. Initially, this participation was limited to the support given by large entrepreneurial leaders to extreme and violent action that the dictatorship used to destroy old institutions and establish new ones (Rebolledo, 2015). Later, large business contribution assumed a leading role in the definition of the new rules of the game embodied in the Constitution of 1980 (Barros, 2004). Once the dictatorship was over, large corporations began to exert influence through the deployment of lobbying activities and by means of attempts (mainly successful) of state capture (Monckeberg, 2002, 2012; Matamala, 2015, Garin 2016).

Large Chilean economic groups have produced significant market shares in the main economic activities by means of that strategy, allowing them to erect automatic and insurmountable barriers to their eventual competitors, at both the input markets and at the markets of final products. The main methods by which certain business actors have been permitted to rapidly move in this direction have been the strong and abrupt increases in their scale of operation by means of the use of two mechanisms:

The first one is the rise in market share implemented through mergers and acquisitions mechanisms, a modality which explains a large part of the market share jump of some large firms. A second but no less important mechanism of concentration has been predation towards smaller competitors, a business practice instituted and consolidated alongside the trade openness process.

In the Chilean case, the thematic of mergers and acquisitions and its history is thoroughly detailed in Appendix III. However, "predatory practices" are analysed in this chapter. They constitute the second factor which explains the drastic reduction in the market

share of the MSME and the increase in the large firm's market share that we have not yet analysed in their complex dynamics.[236]

The concept of "predation" in the business world has already been present in the antitrust literature from the early enactment of the Sherman Acts in the USA (Areeda & Turner, 1975: 697). In this way, certain practices or businesses, as well as pricing strategies, have been defined as "predatory" to the extent that they are subjected to the previously outlined goals. This is particularly true if these practices are developed by firms which are the predator of consumers or companies weaker than themselves. In summary, it can be said that a "predatory business model" is characterised by fulfilling four or more of the following criteria:

In Chile, there is a history of large business behaviours that confirm the presence of the described criteria within the main Chilean business groups, in practically every one of the seven aforementioned areas, as we will describe in detail.

i. **Banking Credit Concentration:** In the year 1990, the participation of large companies in the total banking credit total was 64% of that value (Corfo, 1994), as in 2009 such participation had increased to an 83% (SBIF, 2010), a percentage that seems to evolve following the large firms' market share raise. Additionally, interest rate spreads between loans to SMEs and loans to LSE exhibit clear differences if Chile is compared to other countries of a similar level of development. In a sample of 37 countries, associated and non-associated with the OECD (OECD, 2016), Chile shows a high spread between both destination of banking credits (6.51%), a value that is higher than in any other OECD country and is also on top of the median of the sample (1.36%). The only country in the group with greater credit spread (LEE/SME) than Chile is Colombia, a country that is not a member of OECD and whose GDP is around 60% of the Chilean one.
ii. **Trading Channel´s Concentration:** This situation can be present in any economic sector but is often concentrated in the Sector of Wholesale and Retail trade, towards the end of 2009 the large companies already concentrated 78% of final demand in the economy, a high market share which had been growing steadily since 1990 (SII, 2010). Within the various arrangements thanks to which they have achieved, it is worth noting the role played by commercial

236 In this chapter, their effects will be explored in detail, using the disaggregated analysis of the 2008 IOM.

credit cards issued by large stores. This device is supported in sophisticated arrangements, involving several public financial authorities, and has allowed them to increase their incomes from consumer´s loans. In a short time that loans achieve to exceed the revenues by sales of large retail business operation. The presence of "closed-credit cards" has also been a strategic device of larger trade firms to expand their market share. Retail merchants that have not been able to develop this financing tool have disappeared from the market or have been reduced to very marginal markets. When the users of these credit cards consume the total personals´ liquid incomes, available to serve the obligations with credit card issuers, they can only survive by paying credit quotas that release certain minimum amounts. However, these "new credits" can only be spent on the premises of the retailer who issued the card. This device has produced, during the eighties and nineties, a form of "perfect customer loyalty", constituting one of the main mechanisms through which businesses have been draining the potential market of small retail trade, increasingly concentrating the final demand in only a few trading channels. There are at least two other important arrangements that have enabled the monopolization of marketing channels. One of them is based on the power of the large real state companies associated with the business groups that control the retail sector. They dominate a sophisticated network of lobby companies that have allowed them to design and put into operation new public regulations that allow them to install large shopping centres in the centre of the main cities of Chile. This power has also allowed them to institutionalize regulations that have allowed them to acquire large tracts of land in the best urban locations with commercial potential. They are generally integrated into parking managed by private companies (awarded government contracts), which manage them in areas with affluence of a large number of people, or adjacent to them. In practice, large real estate companies have begun to operate in the neoliberal Chile, as large urban planning entities, which end up defining, for their own benefit, norms and regulations, before which the power of the State, local or national, is extremely reduced. Another important element is the massive practice of price discrimination policies that favour large buyers to the detriment of MSME. The impossibility of establishing in Chile similar legal norms to the Robinson-Patman acts of the USA, puts out of competition the small retailers and distributors and has ended up concentrating them in places of population of low income and low potential of expansion.

iii. **Market Share Concentration:** Between 1990 and 2009, the market share of large Chilean firms, in absolute terms, rose to almost one thousand million USD each year. In the same period, Chile carried out mergers and acquisitions of companies that strongly concentrated its main markets and led the country to have the highest amount of these operations in all Latin America, (25% of GDP) (CEPAL, 2013). The referred concentration is associated, from the neoliberal discourse, to the greater relative efficiency of the LSE, however, in the course of this chapter we will show how, in fact, it rests in a vast network of institutional arrangements that allow the LSE "win the match" even before it starts.

iv. **Erosion of the trade bargaining capabilities of Small companies:** By analogy to a model of industrialisation with an unlimited supply of labour, as described by Lewis (1956), the large Chilean companies act as if placed in a context of virtually "unlimited offer of suppliers of small scale". A small group of companies of around 10,000 firms, demand the bulk of products and inputs produced by the around 700,000 firms of smaller size, increasingly concentrating the trade channels. This situation is based on several arrangements whose orientation has been generating a strong and quasi-monopsonic market power, which allows large companies to control the prices and profits of their client- firms and suppliers. The low trade margins imposed on MSME press them to operate as "minimum-price bidders". After losing their sustainability because of the asymmetric arrangements and negotiations in which they must participate, their trade agreements stop working and are replaced by new small firms with more working capital in condition to be expropriated throughout those mechanisms. This dynamic means that large companies have an almost unlimited reserve of suppliers, enough to replace any of those that do not accept, or cannot run their business by, transferring the main part of their profitability to LSE. This has produced a context in which any process of capital accumulation in MSME tends to be captured by large corporate predators.

v. **Non-Professional Corporate Governance:** About 30 business groups control the 12,000 largest companies. In general, these companies exhibit a family management and ownership, characterized by a low level of professionalism. Most of the Boards of Directors of these companies are made up by members of the family, e.g. their wives, parents, children or direct heirs of the children. They are selected from a circle of family trust, under criteria related to informal relations with the owners, rather than because of their professional competence. Frequently, families hold a majority of shares with right to vote on the board

of directors, thus also controlling the matrix that exerts control of the group, a matrix that is generally made up of non-tradable shares in stock market. The majority of the votes that give the group control can operate either directly or indirectly, but mostly give control to people who can be classified in one or more of the categories previously used to defining the features of a business model. The standard in the area of direct management of the companies within each group, can correspond to one or more professional managers, but at least one representative of the family, participates in the management and government of the company. Finally, it is very difficult to find Chilean economic groups in which, within the company or holding company through which exercise their role as controllers, the person who founded or acquired the company (equity), or relatives or descendants, have less than 25% of the voting rights to which ownership of the capital share is entitled, being frequent that those rights be situated around 60% in companies operating under the figure of closed corporations. In sum, within the corporate governments of about 30 business groups, are tacked family-oriented decisions about the arrangements and operation of at least the 60% of GDP, a power that the Chilean State lack of power to control. This situation lets to see Chilean economy oriented by a hierarchical logic and not by a market one.

vi. **Detachment of any Corporate Social Responsibility Criteria:** The way in which Chile's large business groups assume Social Responsibility with their stakeholders, has been for a long time associated with Milton Friedman's view. This author declared that Business Social Responsibility (BSR) was a "dangerous socialist proposal", because the social responsibility of a business must be to increase its profits. This proposal, operating nowadays, is characterised by the refusal of individual companies to acknowledge the social consequences of their actions. The complement of that perspective is conditioned by several business arrangements. Then, excluded any involvement of firms on social responsibility activities and only develop same kind of social oriented activities, when enterprises receive a tax exemption that lets them transfer to the State the financial weight of that restricted participation in that kind of activities. In general, large firms do not consider the benefit to society and themselves as a result of strengthening the competitive context in which they operate, like "Shared Value" approach suggests (Porter, 2011b) and tend to identify profit maximisation as their major contribution to economy and society.

In sum we can observe that, manoeuvring of the economic groups that develop predatory behaviour is characterized by the development of arrangements directly aimed at constantly harming one or more competitors to improve their market share.

Competition based on merits (efficiency) is not a desirable strategy for them; although it is possible that their businesses have a competitive appearance that does not correspond to the real presence of a competitive environment. A lot of strategic arrangements are used to hide that conduct. To implement these behaviours, economic groups frequently sacrifice short-term benefits, in exchange for expectations of higher profits in the long run, once they have cleared the competition in the markets in which they operate.

The massive implementation by large companies, or conglomerates of these, of a business model having at least four of the seven previously listed features, is a striking characteristic of the Chilean model which, is explained by the sustained growth of the bargaining power of large business. This power is in direct relation, as IOM shows, to the size of their enlarged sales and purchases.

7.5. Spontaneous or Voluntary Institutional Governance of the Chilean System of Business Relationship?

Until now, the evidence provided in this research has not yet answered if institutions that, between 1990 and 2009, have framed the operation of the Chilean economy, are effects or causes of implementation of the Chilean neoliberal model. It is possible to believe that institutions are largely effects of the model and are established, after deployment of autonomous actions of economic agents, when and only when decision makers believe that there are mutual benefits to be gained. On the other hand, it is possible to believe that institutions are important tools of governance but are mainly a reflection of State´s interest, or of private´s interest, operating throughout the State.

We are not in agreement with the first formulation and are very close to the second one.

We think that Chile´s neoliberal model implementation, as has been described in former chapters, was a product of a careful design, partially incubated in the academic world, but mainly within the Chilean State during the dictatorship period. When the monetarist approach, which lead the implementation of first phase of Chilean model, was abandoned, the new approach was an application of a new development

model, incubated first within multilateral agencies and in some leading American Universities, and after that, was adopted as if it were of his property, by the post dictatorship Chilean governments.

The integration of a wide group of institutional arrangements (representing the interest and the power of a tiny group of powerful corporations) within a specific kind of business model whose character we define as "predatory",[237] obey to an intentional political and economic design, and cannot be presented as if it is being a spontaneous and autonomous outcome of the Chilean economic life.

We understand the concept of business model, as a comprehensive and intentional set of institutional arrangements that are not only of economic character, but also of a political character. In the Chilean case, this occurs because institutional actions orientate the implementation of business arrangements, possess a sort of orientation role (of politico-cultural character), because the neo-liberal view who constitute such business model, constitute a paradigm who orientate the way in which the current business arrangements should be protected and future arrangements should be implemented.

From our perspective, the predominant business model, which we will characterise in this chapter, is associated with a specific form of governance of the Chilean markets. This governance of neoliberal character is not considered by us as a tool oriented to minimise the transactional costs of the Chilean economy and thus maximise its efficiency, on the contrary, as we show in this chapter, their role is clearly different.

7.6. The Governance Institutions and the Remuneration-Productivity Gap

Given the availability of CASEN data (Surveys CASEN 1990-2009) which provides very detailed statistics about employment, it was possible for us to disaggregate companies by size. From there, it is clear that the enterprises of largest size and productivity are the only ones that increase their participation in employment, while the three remaining formal firm's strata significantly reduce it.

237 A relationship between two persons or entities, must be defined as predatory when one of them treat to the other badly for your own benefit. This concept in the business world is used relating to companies that are looking for other companies to buy, or are showing the described type of behaviour. (see, https://www.macmillandictionary.com/dictionary/british/predatory)

As is visualised in Figure 7.1, large enterprises have raised their employment absorption capacity during the analysed period, during 1990 to 2009, they have passed from possessing 19% of the total employment of economy, to 27%, which means moving from producing 32% to 42% of the formal employment of the economy. According to neoclassical and neoliberal vision, in the Chilean economy, these figures would display a trend towards the replacement of low productivity employment with high productivity employment. Particularly from the neoliberal viewpoint, this tendency evaluated by them as "progressive", has been associated with trade openness and denominated by them as "a successful path of economic modernization", which they believe characterises the country (Buchi, 2008; Galetovic et al 2009).

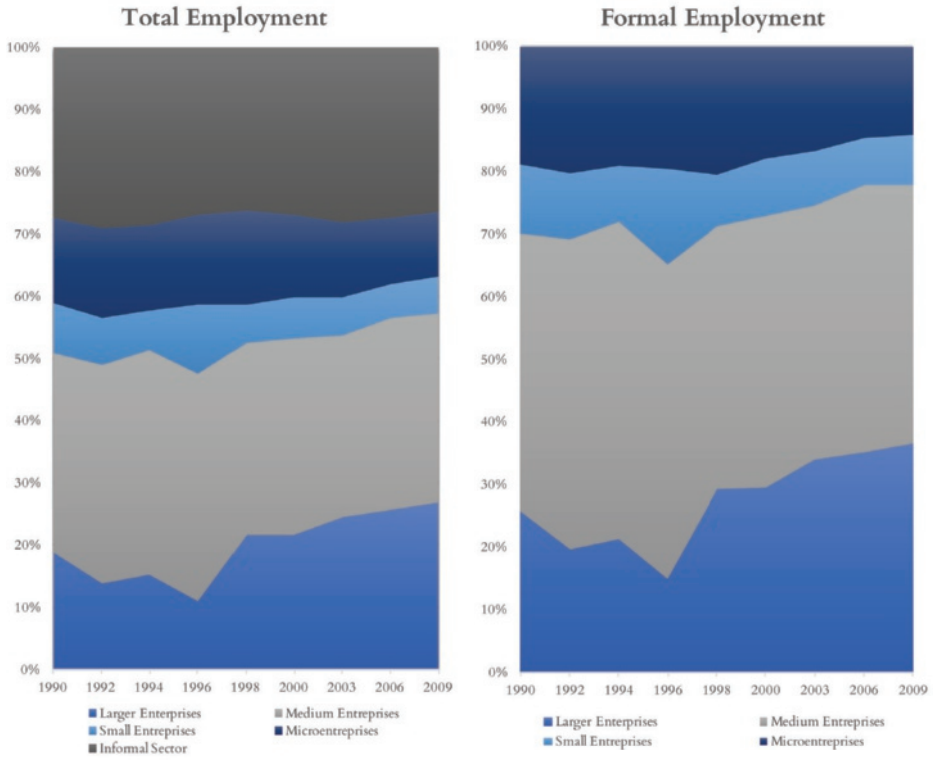

Figure 7.1. Total Employment Produced in the Chilean Economy 1990–2009 by Size Strata and Occupational Category.
Source: Author´s elaboration based on micro data of CASEN Surveys: 1990–2009.

Analysts outside of the mainstream profess the contrary view, assessing that this trend would simply be a by-product of the erosion of market competition induced by larger enterprises. However, to make that neoliberal projection conform to reality, workers

relocated to higher scale firms should increase their productivity and remunerations in their new jobs. Otherwise, maintaining the levels of production of the larger enterprises, but increasing their number of employees, or whether companies increase their production less than proportionally to the increase in their number of employees, the outcome would be a global drop in the productivity of the larger companies and of the economy as a whole, given the weight of LSE within the GDP

To the extent that small firms continue approaching their wage level to their productivity, such wages would increasingly come close to the salaries of large corporations, pushing up the latter. However, the trend has operated in the contrary direction. The reduction of the market share of small companies and the increase of the market share of large companies, has strongly reduced the wages paid by the small companies. This has resulted in wage depression in the large companies. LSE´s use the surplus of cheap labour which, due to this process, has been formed in small companies and that allows significantly reduced wages within large companies. That is possible because, in addition to their power over labour demand, large corporations (as we show in this chapter) also control the final demand of goods and services, and the demand for intermediate inputs.

The leading neoclassical and neoliberal explanations about the persistence of this remuneration-productivity gap among sizes of firms, emphasises the lack of schooling (low human capital) and the scarcity of access by some social sectors to quality education. Another alternative neoclassical explanation accentuates the presence of a divorce between wages and productivity because of the presence of a favourable wage structure for the tertiary levels and post-graduate education, which only a tiny fraction of the population can obtain (Connolly and Gottschalk, 2006).

In the Chilean case, it is very difficult to demonstrate that human capital quality is the main determinant of labour productivity gap between sizes of firms. Perhaps human capital would affect productivity through its interaction with trade orientation, but only if trade openness fosters competition encouraging the use of modern technology, especially in the backward sectors, increasing the demand for high-skilled labour, promoting *learning by doing* and remunerating labour in a manner attuned to their eventual productivity rise. However, several studies about Chilean human capital markets have seriously questioned the hypothesis that posits a beneficial relationship between the quality of human capital and compensations. These studies show that despite similar levels of education, the remuneration of Chilean persons of more modest

social origin, tends to be well below the remunerations of their colleagues from more affluent social origins (Engel y Navia; 2006).

In the same vein, Gutiérrez and Núñez (2004), using a data rich in measurements of the several generating capabilities of productivity and the differentiation of social classes, found that Chilean upper-class professionals earn roughly 50% more than those who have grown up in other socio-economic strata. This gap is not related to differences such as their academic performance in college, their command of a second language, their graduate studies, or the academic quality of schools where they have studied – this suggests the presence of some form of discrimination.[238] Those researchers suggest that human capital gaps are not the cause of the scrawny outcomes of the neoliberal model. On the contrary, they mainly would be consequences of the articulation of some forms of discrimination and the growing market power of LSE based on institutions of governance affecting the distribution of income and the distribution of employment. Those institutions would be the origin of the boundaries imposed to generation of value and innovation in the economy.

In our vision, the cited institutions of governance in Chile assume the form of a specific "business model" that concentrates the whole of institutional arrangements. Meaning that, the dynamic set by formal and informal regulations and networks, shaped by economic exchange, socio-cultural norms and political regime, and which generally provide welfare, identity, solidarity and sense of belonging, have in the Chilean case produced inequality, low productivity, stagnation of growth process and natural resource degradation.[239]

If we analyse issues related to Chilean institutional arrangements, from a structural point of view as well as from features of their actor-oriented aspects, our analysis must be focused to reflect three analytical dimensions (Granovetter, 1985): (a) access to resources, information, power and networks, (b) rights, rules and responsibilities regarding governance regimes, and (c) identity, culture and sense of belonging.

238 In the labour market, "discrimination" imply make discretional distinctions about remunerations, based on spurious considerations like the racial origin racial, sex or socioeconomic level,

239 A synthetic definition and description of the main modalities of institutional arrangements can be found at CIDI (2007).

We estimate that conformation and implementation of a business model, include an articulation of all those aspects within a comprehensive framework. Of course, a business model does not exert all time a direct influence beyond the economic arena, moreover, it is possible that their indirect influence on the cultural, social and political arena may be not minor, and it receives more influences from those areas than the influence that it exerts over them. However, it is a fact that, when we develop an institutional analysis of Chilean economy, the dominant business model appears as a key factor of it.

The analysis of matters related to the first already cited three analytical dimensions, provides understanding of opportunities and constraints that neoliberal business model provides to firms, of any size or productivity level, operating in the Chilean markets. Implications of those issues for poverty elimination uphill struggle and for inequality reduction laborious task are very clear.

Issues related to second analytical dimension, captures the internal organisation and external linkages that demarcate the role of neoliberal business model as a part of a context of continuous struggles between economic and social agents. This dimension includes all specific market arrangements which are described and analysed in this chapter. The third analytical dimension refers aspects of (in)formal embedment of the business neoliberal model that give rise to (I) inclusion or exclusion (of firms and individuals) in the potential gains associated to trade openness and market liberalization, (ii) the motivations for fighting or underwrite prevailing institutional arrangements, accepting or refusing their impact on citizenship at agency level (CIDI, 2007). This last dimension includes the remaining institutional arrangements that make up the institutional governance of the Chilean economy and make part of areas wider than mere market relations.

Verbalized that point, the relevant questions are:

1. In Chile, shapes and features assumed by the institutions of governance, are a dispersed body of private arrangements independently produced, or make part of an economic and political design implemented from the State?
2. Do they obey the outcomes of the Chilean model, to distortions, frictions and laggards of the opening and liberalization process, or can we talk of a failure in the entire line of neoliberal projections about the efficiency of their development model?

In this chapter, we will try to answer both questions, analysing those issues from the three analytical dimensions already explained.

7.7. The Chilean Input–Output Matrix Disaggregated by size

The IOM analysis used in this study, will allow us to review more accurately not only the outcomes of the Chilean model in terms of conformation of linkages and economic relationships among different sizes of firms, but also understand the integrity of relationships established among economic actors.

By this way will be possible understand the presence of institutional arrangements in the productive fabric and the real impact of them in production, consumption and distribution of value added. In the input-output model, the analysis of changes in the productive structure has a long tradition (Leontief 1955; Chenery, Shishido et al 1962; Carter, 1970; Stäglin and Wessels, 1972 and Bullmer-Thomas, 1978). During the 1980s, this type of analysis again experienced a boom due to the contributions of Wolff (1985), Feldman, McClain et al (1987) and Skolka (1989).

In our analysis, the focus has been upon decomposition techniques, which have become an important tool to unravel the sources of temporary growth of certain variables, allowing the separation of these sources into their constituent parts. The use of structural decomposition techniques enables the quantification of the sources of change underlying a wide variable range.

For example, this includes: production levels (Fujimagari, 1989), added value (Oosterhaven et all, 1994), energy use (Lin and Polenske, 1995), employment needs (Forssell, 1988) imports volume (Kanemitsu and Ohnishi, 1989), production of the services sector (Barker, 1990) or total inputs requirements (Casler et al, 1991, 1996), all focused at the sector level.

Following this line of enquiry, we proceeded to use the disaggregation techniques of IOM to identify, at the intermediate level, the flows of economic activities classified according to different productivity levels, as well as other issues derivate from the distribution of value-added and final demand of these activities/sectors.[240]

240 The general methodology for the identification of economic linkages, according to productivity levels, was developed in this study from the base information provided by the observed economic

On that basis, in the course of this study, several tasks were carried out which allowed us to characterise existing linkages between the different strata of Chilean company sizes, their differential capacity to generate added value, the primary distribution of income in its interior, as well as the issues derived from the relations between companies of different sizes. All these tasks were advanced in order to determine the effect of each stratum and sector of different size firms on the performance of the Chilean economy

7.8. The Sectorial Economic Relationships of Chilean Economy

The Central Bank of Chile uses an input-output matrix (IOM) which updates periodically as a tool to identify the observable structure of the Chilean economy (BCCH, 2008).[241] The latest version of the IOM, published in 2011, records inter-sectorial linkages existing in 2008. It provides a detailed picture of the country's economic structure during the last years of our period of analysis.[242]

In our study, the IOM analysis was used to identify the economic relationship existing between activity sectors and different sized companies.

With that purpose, we built nine by nine sectors IOM of the Chilean economy, which is displayed in Table 7.1. (A) In which figures are expressed in Chilean pesos of year 2008. Figures reported at table 7.1. (B) Are displayed as shares of different kinds of utilization (intermediate and final) recorded on Table 7.2. (A), estimated on total GVP.

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interrelations in the available input-output matrixes. In particular, the most recent input-output tables published by the Central Bank of Chile in 2006 and 2011. Additionally, we used information from the National Industrial Survey ENIA: 1990 / 2011, INE; Socio-economic Characterization Households Survey CASEN 1990 / 2011; Database of Company Tax payers, from the SII. Database of Exporting Chilean Companies, NCS-DNA; Input Product Matrixes of Chile, 2003-2008; National Employment Surveys (INE).

241 The input-output matrix 2008 has allowed us to identify economic, demand and supply flows between the economic agents of the Chilean economy, expressed through a set of double entry tables, in which the production obtained by the different economic activities were registered in the tables and its respective intermediate or final use in the columns.

242 Given the low variability of technical coefficients of the IOM (VA/ GVP and IC/GVP), in general it is fair to assume (like the central Bank does) that the characteristics of the Chilean economy registered therein, are valid for a period covering less three years before its preparation and three years after.

Tables 7.2. (A) and 7.2 (B), display an IOM disag**gre**gated by sectors. All their components, e.g. their intermediate utilisation (domestic and imported), their final utilization and the value-added components. The data in these tables shows supply side (production) on its vertical axis and demand side (utilisation) on its horizontal axis. The supply side show is presented disaggregated into nine sectors, differentiating the utilization of domestic inputs from the utilization of imported inputs.

Additionally, value added is disaggregated into four components that describe distribution of value added among two different kinds of taxes and the remuneration of two factors of production, capital and labour.

The final demand included a registry of consumption of the government and non-profit private organisations, changes in inventories, gross fixed capital formation and export sector which (as a destiny segments) are presented without disaggregation of any kind. Additionally, is presented the households´ consumption of goods and services; that was disaggregated into three layers, defined according to its respective per capita income level: high, middle and low.[243]

Tables 7.1. (A and B) reflect the sectorial structure of the economy towards the end of the analysed period and show the result of thirty-five years of trade liberalization. The first table present its figures in absolute values, but in the second table the same figures are presented as percentages of GVP. However, from both sources, we can observe that the Chilean economy is far from being diversified or demonstrating increased levels of added value in production

243 The stratum that we denominate as "lower consumption" was associated to 1 to 4 deciles, the "medium consumption" to 5 to 7 deciles and the "high consumption" to 8 to 10 deciles.

Table 7.1. (A). Input - Output Matrix Chilean Economy 2008

	Intermedial Utilization									
Components of GVP	AFF	M&Q	MAN	EGA	CONST	WRT	TR	FIA	SCS	Total IU
Agriculture, forestry and fishing	634	10	4.915	46	3	206	13	80	31	5.938
Mining and quarrying	36	1.980	1.444	23	84	32	4	46	0	3.648
Manufacturing	1.679	1.484	5.494	714	3.444	1.643	1.120	926	839	17.342
Electricity, gas and water supply	97	1.232	1.193	3.817	86	373	176	303	447	7.724
Construction	16	18	76	80	11	152	113	152	1.274	1.893
Wholesale and retail trade	502	357	1.526	116	968	1.076	822	570	482	6.419
Transport	203	439	1.599	189	162	1.920	2.706	835	353	8.407
Financial and insurance activities	1.066	1.418	3.660	258	1.596	3.929	1.950	5.526	1.833	21.236
Social and community services	29	31	254	23	10	79	32	119	565	1.140
Domestic Intermediate Consumption	4.261	6.968	20.160	5.267	6.365	9.409	6.935	8.555	5.826	73.747
Agriculture, forestry and fishing	136	0	416	2	0	15	1	22	3	595
Mining and quarrying	15	205	4.054	658	13	93	11	22	0	5.071
Manufacturing	809	1.186	5.387	891	1.486	754	2.338	805	522	14.180
Electricity, gas and water supply	0	0	0	28	0	0	0	0	0	29
Construction	0	0	0	0	0	0	0	0	0	0
Wholesale and retail trade	3	20	217	2	0	26	18	3	9	298
Transport	1	0	22	0	1	24	1.510	72	14	1.645
Financial and insurance activities	3	97	199	102	11	140	212	619	58	1.441
Social and community services	0	0	6	0	0	2	69	14	23	115
Imported Intermediate Consumption	967	1.509	10.302	1.684	1.512	1.054	4.159	1.558	630	23.374
Total , Intermediate Consumption	5.228	8.477	30.462	6.951	7.877	10.463	11.095	10.113	6.456	97.121
Taxes	10	1	18	1	9	24	411	530	516	1.520
Other Taxes	78	18	158	6	106	334	-81	253	573	1.445
Operating surplus	1.589	10.760	6.490	2.201	3.534	3.563	4.127	10.359	6.736	49.359
Labour Remunerations	1.289	1.527	3.823	319	3.268	4.668	2.211	6.847	10.181	34.133
Total Value Added	2.965	12.306	10.490	2.527	6.916	8.589	6.668	17.988	18.006	86.457
Gross Value of Production	**8.193**	**20.784**	**40.952**	**9.478**	**14.793**	**19.052**	**17.763**	**28.101**	**24.462**	**183.578**

Source: Author´s elaboration based on the IOM 2008 (CCNN-CDR; 2011).

Final Utilization									Total GVP (IU+FU)
	Households								
Government	Low Income,	Medium Income	High Income	Non Profit Private Org.	Changes in inventories	Gross Fixed Capital Formation	Exports	Total FU	
18	255	274	371	0	-97	255	1.180	2.255	8.193
0	0	0	0	0	-89	0	17.224	17.135	20.784
48	1.982	2.610	4.777	0	877	789	12.526	23.609	40.952
35	461	493	764	0	0	0	0	1.754	9.479
0	0	0	0	0	0	12.900	0	12.900	14.793
164	1.541	2.258	5.594	0	8	1.604	1.466	12.634	19.053
0	967	1.470	2.972	0	0	0	3.948	9.356	17.763
161	232	477	4.270	0	0	1.001	723	6.865	28.101
10.069	1.588	2.632	7.501	717	3	-150	962	23.321	24.461
10.495	7.025	10.213	26.250	717	702	16.399	38.028	109.831	183.578
0	15	17	25	0	6	3	0	65	661
0	0	0	0	0	88	0	2	90	5.160
0	885	1.415	3.752	0	388	5.805	923	13.167	27.347
0	0	0	0	0	0	0	0	0	29
0	0	0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0	298
0	8	19	182	0	0	0	0	210	1.854
0	2	4	9	0	0	250	0	265	1.705
0	39	71	390	0	0	4	0	505	621
0	949	1.526	4.358	0	481	6.062	925	14.302	37.675
10.495	7.974	11.740	30.608	717	1.184	22.462	38.953	124.132	221.253
58	945	1.403	3.695	0	0	717	0	6.818	8.338
								0	1.445
								0	49.359
								0	34.133
58	945	1.403	3.695	0	0	717	0	6.818	93.275
10.553	8.919	13.143	34.303	717	1.184	23.179	38.953	130.950	**314.528**

Table 7.1. (B). Input-Output Matrix Chilean Economy 2008 (Components as a Proportion of Total GVP)

	Intermedial Utilization							
Components of GVP	AFF	M&Q	MAN	EGA	CONST	WRT	TR	FIA
Agriculture, forestry and fishing	0,0774	0,0005	0,1200	0,0049	0,0002	0,0108	0,0007	0,0028
Mining and quarrying	0,0044	0,0953	0,0353	0,0025	0,0057	0,0017	0,0002	0,0016
Manufacturing	0,2049	0,0714	0,1342	0,0754	0,2328	0,0862	0,0630	0,0329
Electricity, gas and water supply	0,0118	0,0593	0,0291	0,4027	0,0058	0,0196	0,0099	0,0108
Construction	0,0020	0,0009	0,0019	0,0085	0,0007	0,0080	0,0063	0,0054
Wholesale and retail trade	0,0613	0,0172	0,0373	0,0122	0,0654	0,0565	0,0463	0,0203
Transport	0,0248	0,0211	0,0390	0,0199	0,0110	0,1008	0,1524	0,0297
Financial and insurance activities	0,1302	0,0682	0,0894	0,0273	0,1079	0,2062	0,1098	0,1966
Social and community services	0,0035	0,0015	0,0062	0,0024	0,0007	0,0041	0,0018	0,0042
Domestic Intermediate Consumption	0,5201	0,3353	0,4923	0,5556	0,4303	0,4939	0,3904	0,3044
Agriculture, forestry and fishing	0,0166	0,0000	0,0102	0,0002	0,0000	0,0008	0,0000	0,0008
Mining and quarrying	0,0019	0,0099	0,0990	0,0694	0,0009	0,0049	0,0006	0,0008
Manufacturing	0,0988	0,0571	0,1315	0,0941	0,1005	0,0396	0,1316	0,0287
Electricity, gas and water supply	0,0000	0,0000	0,0000	0,0030	0,0000	0,0000	0,0000	0,0000
Construction	0,0000	0,0000	0,0000	0,0000	0,0000	0,0000	0,0000	0,0000
Wholesale and retail trade	0,0003	0,0010	0,0053	0,0002	0,0000	0,0014	0,0010	0,0001
Transport	0,0001	0,0000	0,0005	0,0000	0,0001	0,0013	0,0850	0,0025
Financial and insurance activities	0,0004	0,0047	0,0049	0,0108	0,0007	0,0073	0,0119	0,0220
Social and community services	0,0000	0,0000	0,0002	0,0000	0,0000	0,0001	0,0039	0,0005
Imported Intermediate Consumption	0,1180	0,0726	0,2516	0,1777	0,1022	0,0553	0,2342	0,0554
Total Intermediate Consumption	0,6381	0,4079	0,7439	0,7334	0,5325	0,5492	0,6246	0,3599
Taxes	0,0012	0,0001	0,0004	0,0001	0,0006	0,0013	0,0232	0,0189
Other Taxes	0,0095	0,0009	0,0039	0,0006	0,0072	0,0175	-0,0046	0,0090
Operating surplus	0,1939	0,5177	0,1585	0,2323	0,2389	0,1870	0,2324	0,3686
Labour Remunerations	0,1573	0,0735	0,0934	0,0337	0,2209	0,2450	0,1245	0,2437
Total Value Added	0,3619	0,5921	0,2561	0,2666	0,4675	0,4508	0,3754	0,6401
Gross Value of Production	**1,0000**	**1,0000**	**1,0000**	**1,0000**	**1,0000**	**1,0000**	**1,0000**	**1,0000**

Source: Author´s elaboration based on the IOM 2008 (CCNN-CDR; 2011).

			Final Utilization									Total GVP (IU+FU)
			Households									
SCS	Total IU	Government	Low Income,	Medium Income	High Income	Non Profit Private Org.	Changes in inventories	Gross Fixed Capital Formation	Exports	Total FU	
0,0013	0,0323	0,0017	0,0285	0,0209	0,0108	0,0000	-0,0823	0,0110	0,0303	0,0172	0,0260
0,0000	0,0199	0,0000	0,0000	0,0000	0,0000	0,0000	-0,0752	0,0000	0,4422	0,1309	0,0661
0,0343	0,0945	0,0046	0,2222	0,1986	0,1393	0,0000	0,7413	0,0340	0,3216	0,1803	0,1302
0,0183	0,0421	0,0034	0,0517	0,0375	0,0223	0,0000	0,0000	0,0000	0,0000	0,0134	0,0301
0,0521	0,0103	0,0000	0,0000	0,0000	0,0000	0,0000	0,0000	0,5566	0,0000	0,0985	0,0470
0,0197	0,0350	0,0155	0,1728	0,1718	0,1631	0,0000	0,0069	0,0692	0,0376	0,0965	0,0606
0,0144	0,0458	0,0000	0,1084	0,1118	0,0867	0,0000	0,0000	0,0000	0,1013	0,0715	0,0565
0,0750	0,1157	0,0153	0,0260	0,0363	0,1245	0,0000	0,0000	0,0432	0,0186	0,0524	0,0893
0,0231	0,0062	0,9541	0,1780	0,2003	0,2187	1,0000	0,0027	-0,0065	0,0247	0,1781	0,0778
0,2382	0,4017	0,9945	0,7877	0,7771	0,7652	1,0000	0,5933	0,7075	0,9763	0,8387	0,5837
0,0001	0,0032	0,0000	0,0016	0,0013	0,0007	0,0000	0,0048	0,0001	0,0000	0,0005	0,0021
0,0000	0,0276	0,0000	0,0000	0,0000	0,0000	0,0000	0,0740	0,0000	0,0001	0,0007	0,0164
0,0214	0,0772	0,0000	0,0993	0,1076	0,1094	0,0000	0,3278	0,2504	0,0237	0,1005	0,0869
0,0000	0,0002	0,0000	0,0000	0,0000	0,0000	0,0000	0,0000	0,0000	0,0000	0,0000	0,0001
0,0000	0,0000	0,0000	0,0000	0,0000	0,0000	0,0000	0,0000	0,0000	0,0000	0,0000	0,0000
0,0004	0,0016	0,0000	0,0000	0,0000	0,0000	0,0000	0,0000	0,0000	0,0000	0,0000	0,0009
0,0006	0,0090	0,0000	0,0009	0,0015	0,0053	0,0000	0,0000	0,0000	0,0000	0,0016	0,0059
0,0024	0,0078	0,0000	0,0002	0,0003	0,0002	0,0000	0,0000	0,0108	0,0000	0,0020	0,0054
0,0009	0,0006	0,0000	0,0044	0,0054	0,0114	0,0000	0,0001	0,0002	0,0000	0,0039	0,0020
0,0257	0,1273	0,0000	0,1064	0,1161	0,1270	0,0000	0,4067	0,2615	0,0237	0,1092	0,1198
0,2639	0,5290	0,9945	0,8940	0,8932	0,8923	1,0000	1,0000	0,9691	1,0000	0,9479	0,7034
0,0211	0,0083	0,0055	0,1060	0,1068	0,1077	0,0000	0,0000	0,0309	0,0000	0,0521	0,0265
0,0234	0,0079										0,0046
0,2754	0,2689										0,1569
0,4162	0,1859										0,1085
0,7361	0,4710	0,0055	0,1060	0,1068	0,1077	0,0000	0,0000	0,0309	0,0000	0,0521	0,2966
1,0000	**1,0000**	1,0000	1,0000	1,0000	1,0000	1,0000	1,0000	1,0000	1,0000	1,0000	**1,0000**

From these two tables, we can see that in 2008, the Chilean economy produced a gross value of production (GVP) of 183,578 billion pesos. If we disaggregate that figure from the demand side (destiny of production) 97,121 billion (53%) corresponded to inputs intermediate utilisation and 109,831 billion (47%) to final utilisation. From this last item, 10,495 billion corresponded to government consumption (6%), 43,488 billion to household consumption, 717 billion to non-profit private organisation consumption (0,39%), 702 billion to changes in inventories (0,38%), 16,399 billion to gross investment in fixed capital (8,93%) and 38,028 to inputs used by the export sector (20,72%).

If we disaggregate GVP from the demand side, in Tables 7.1. (A) and 7.1. (B), we can also see that, within the of GVP, that the value of intermediate inputs utilised were 97.121 billion; that means 52,9% of GVP (73,747 billions of domestic origins [40,17%] and 23.374 imported [12,73%]).

On the other hand, the value added (VA) reached 86,457 billion (47,1% of GVP). That figure includes 1,520 billion in general taxes and 1,445 in other taxes (in total 1.6% of GVP), 49,359 billion in operating surplus or capital remuneration (27% of GVP) and 34,133 billion in wages (19% of GVP).

As can be also seen from these figures which, within the production produced, the use of domestic intermediate inputs is strongly concentrated in three sectors: Manufacturing 9,45% (17.342 billion) Wholesale and Retail Trade 3,5% (6.419 billion) and Financial and Insurance 11,57% (21.236 billion). This last sector provides inputs amounting to 3,660 billion to the Manufacturing sector (1,99%); 3,929 billion to the Retail and Wholesale Trade sector (2,14%) and 5,526 billion to itself (3,01).

The only three cross transactions of certain scale, in addition to those already listed, come from the agricultural sector, which supplies 4,915 billion to the manufacturing sector, which supplies itself with inputs whose value amounts to 5,494 billion annually and the electricity, gas and water supply which, in turn, also supplies itself with inputs whose value amounts to 3,817 billion.

As shown by these figures, which reflect the sectorial structure of the economy towards the end of the analysed period and show the result of thirty-five years of trade liberalization, the Chilean economy is far from being diversified or demonstrating

increased levels of added value in production.[244] On the contrary, if we observe the final utilization of goods and services, manufacturing, financial sector, export-mining sector and social and community services are which plays a decisive role.

If we consider the origin of production, (supply side) situation is not much better.

The Value Added (VA) contained in the GVP of the economy amounts to 47% of it and within VA the taxes are equivalent to 2% of the GVP, insofar as the Operating Surplus is 27% of the GVP and the labour remuneration 19%. On the other hand, Total Intermediate Consumption (TIC) is 53% of GVP. Within it, utilization of domestic inputs is equivalent to 41% of GVP and imported inputs utilization is equivalent to 13% of GVP).

The ratio (VA/GVP) reflects the proportion of value added existing into GVP (The technical coefficients of IOM). It is known that a country that has a higher quotient VA/GVP than another one, reflects that it is possible to it obtain a higher level of VA (than another country) with the same level of GVP. In other words, the first country would have higher productivity. Using the same reasoning, for the same level of GDP, a high level of VA means that Intermediate Utilisation is lower.

A lower intermediate utilisation allows a country to obtain higher levels of GDP with bigger efficiency and vice versa if intermediate utilization is smaller. Whilst in Canada, the ratio IU/GVP is 48.1%, in the USA it is 46.2%, and in Mexico 42.4%. Chile exhibits values higher than all of these because it needs to use as intermediate consumption a 52.9% of each unit of GVP. A situation that only may express low levels of efficiency in relation to countries with which it may be compared.[245]

This first information extracted from IOM data, clearly displays the contradictory results of four decades of economic openness informed by neoliberal perspectives.

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244 If we compare figures of Chile´s IOMs (2003-2008) share of VA on GVP fall over 6% in five years.

245 When we observe the quality of sectorial use of resources, we can see that Chile presents a low productive efficiency in relation to any comparative OECD country. Chilean Value Added/ Gross Value of Production quotient is 47,1 %, but the Canadian is 51.9% and the USA quotient is 53.8%, both of them far superior to the Chilean one (IMF, 2010). However, if Chile is compared with other OECD countries, which like Mexico are less developed than Chile, we find that the quotient VA/GVP of that country (57.6%) is well aligned with the quotient of developed OECD countries, being widely superior to the Chilean one.

Chile has not yet become a modern and efficient export-led economy. In spite of its radical trade openness, Chile continues being an economy focused on domestic market. From the IOM, it is easy to visualise which, in practically all sectors that are intensive in the use of natural resources to produce commodities, concentration predominates over diversification and those sectors dominate today's economic activity. Furthermore, traditional export sectors (e.g., mining sector) continue playing a role similar to that played by them during the period of import substitution, before the implementation of the neoliberal model, while trade liberalization has exerted too much influence on its dynamics.

The openness outcomes appear contradictory. The economic dominance of non-tradable sectors and the progress focused only in primary tradable goods that are highly intensives in natural resources whose export is mainly guaranteed by their particular characteristics, has not been the promised outcome of neoliberalism. Moreover, in general, a successful primary export process such as Chile displays, surely does not need any process of openness and liberalisation
At the sectorial level, the main sector is the Manufacturing industry.

This sector has a production that is highly intensive in natural resources of low elaboration playing a leading role, producing goods of a value of 40,952 billion representing 22.3% of Chilean GVP. Manufacturing intermediate utilization is 17,342 billion and final utilization 23,609 billion.

This last figure is composed by 48 billion of governments consumption, 9,638 billion consumed by households, 12.526 billion are exported goods and changes in inventories and gross capital formation constitute the remaining 1.7 billion. Within the manufacturing sector, the share of industrial products of high value added is not so relevant, predominating products like paper and cellulose, derivate from oil, and food and tobacco products.

The second main sector, within GVP, is Insurance and Banking Services sector which produce 28,101 billion, representing 15.31% of GVP, a situation which, reflect the high cost of financial services provided by it to other economic sectors.[246]. Chilean

246 Comparing Active Interest Rates (AIR), which are those that banks charge for loans to first line customers, the 2008 average of all the countries for which there is information, was 13.35% yearly. The AIR of Japan was the lowest in the world (2.0), but USA, UK and Holland, recorded annual rates of 5.0. Meanwhile, Chile recorded that year an AIR of 13.0, equal to that recorded by Albania (source: www.

capital market is highly concentrated, and during 2008, commercial banks accounted for 77% of the sectorial services production of this sector and the four major banks owned 66% of the banking assets (BCCH, 2011). The main products of the financial and insurance sectors are the management of financial risks, the provision of liquidity, financing of insurance plans, risk management and the explicit transformation of liquidity in exchange for financial commissions.

The third main sector is mining (20,784 billion) that represent 11.3% of GVP and 16% of Chilean exports (17,224 billion over total exports of 38,028 billion). Lastly, Social and Community Services represent a 13.3% of GVP (24,461billion). However, this last figure is essentially constituted by services provided by public administration whose main utilization, (41% of GVP) correspond to the central government (10,069 billion) (5.7% of GVP) and High Incomes Households representing 4.1% of GVP (7,501 billion). Because the expansion of this sector is a function of public spending which, in turn, depends on the production´s growth of the remaining sectors of the economy, we do not consider that sector as one of qualitative relevance

From these figures, it is clear that trade openness and market liberalisation process has not led to strengthening of a virtuous relationship between production of high added value and strong export orientation. Neither has it oriented industries that participate in global markets to obtain world class inputs and technology that allow them to improve export performance. On the contrary, the openness and liberalization process has resulted in the growing dominance of afore mentioned sectors over the rest of the economy, an issue which is disclosed by the share of sectorial production value of these segments on the Gross Value of Production of economy as a whole.

However, even IOM gives us a clear general picture of Chilean economy, that is not enough for our purposes, which is to inquire about the outcomes of institutional arrangement among different sizes of firms. Because that, before advancing more conclusions, we believe that it is necessary to make deeper our analysis of economy by means of a further IOM disaggregation.

Clarified sectorial relationships existent in Chilean economy and also relations and dimensions of components of GDP, in next part of this chapter, this IOM is unbundled according to size of companies (Small, Medium and Large). This will be used to build

TheGlobalEconomy.com), something difficult to explain in an economy with a fully open financial account.

matrixes broken down by size of firms, in order to construct a Structural Economic Matrix of the Chilean Economy (SEM) for the year 2008.

That SEM will be utilised to identify the flows of intermediate economic activities classified according to different productivity levels (associated to size of firms), as well as the distribution of value-added and final demand of these activities/levels.[247] These economic relations and distributions of GVP, Value Added, Intermediate Consume and Final Demand, are a direct result of each particular institutional arrangement and therefore will illustrate not only the presence of these, but above all their results

7.9. The Size´s Sectorial Economic Relationships of Chilean Economy

The analysis of structural relationships between different segments of enterprises, between sectors and within them, required the identification of the intermediate flows between economic activities, as well as between those and the final demand components, disaggregated by size.

For that reason, the original IOM necessitated some changes in the recorded data, in order to visualize both kinds of flows. Thenceforth the construction of a new matrix presentation, disaggregated by sizes of firms, is needed for register properly that flows and to made possible evaluate outcomes produced by market arrangements.

Intermediate transactions and final consumption between the three sizes of companies in each sector (small, medium and large) with each of the three sizes of companies in other sectors, can be viewed on the next tables (7.2.A and 7.2.B). This information enables you to identify these relationships both at the level of intermediate consumption and value added as of the final demand. In these tables is possible to visualize cited relationships for intermediate consumption of domestic origin, of imported origin and for the sum of two kinds of intermediate consumption.

It is also possible to observe therein the demand of households targeted by income levels of households (low, medium and high), as well as the origin of final goods and

247 This work is reported in Appendix V. Report included description of 12 stages characterised by a documentary product. Each document consists of an Excel or Access file. Following their sequence, it is possible to reach the estimates reviewed here.

services demanded by each one of the three types of households, coming from each one of this three types of firms in every sector of the economy. The same exercise can be done for the remaining components of the Final Utilisation.

From this information will be possible to view the aggregate impact of these interrelationships in the generation of value added of the economy. Unfortunately, in Chile there is no accurate information that allows in turn to segment, from the supply side (rows), the value-added taxes or factor remuneration by the size of companies.

However, our methodology of breakdown allowed us to do so from the demand side (columns), so each one of the components of the value added of the economy was vertically unbundled by the size of company, for each sector of the economy.

Given the size of the IOM, in order to facilitate its reading, in a first phase, the matrix has been divided into fourth arrays.

1. One array shows the relations at the level of Domestic Intermediate Utilization (7.2 (A))
2. The second shows the Imported Intermediate Consumption (7.2. (B)),
3. The third array shows relationships at the level of Final Demand (7.2. (C))
4. The fourth array shows relationships at the level of the Value Added of the economy (7.3.)

Table 7.2. (A). Matrix of Inter-Sectorial and Size Relationships of the Chilean Economy.
Domestic Intermediate Utilization.

				INTERMEDIATE UTILIZATION BY SECTORS AND SIZE. (I)						
				Agriculture, forestry and fishing			AFF	Mining and quarrying		
Production	Domestic Production	SMALL	AFF	68	0	5	73	0	0	3
		MEDIUM	AFF	0	0	1	1	0	0	1
		LARGE	AFF	232	8	320	560	0	0	6
			AFF	300	8	326	**634**	**0**	**0**	**10**
		SMALL	M&Q	0	0	0	0	0	1	0
		MEDIUM	M&Q	0	0	0	0	0	0	0
		LARGE	M&Q	0	27	8	36	0	1	1.977
			M&Q	0	27	9	36	0	2	1.977
		SMALL	Manuf	1	1	8	9	0	0	4
		MEDIUM	Manuf	506	1	566	1.073	0	0	1
		LARGE	Manuf	128	138	331	597	3	17	1.459
			Manuf	634	140	904	1.679	3	17	1.464
		SMALL	EGW	0	0	0	0	0	0	0
		MEDIUM	EGW	0	0	0	0	0	0	0
		LARGE	EGW	50	21	25	97	0	38	1.194
			EGW	50	21	25	97	0	38	1.194
		SMALL	Construc.	0	0	0	0	0	0	0
		MEDIUM	Construc.	0	0	0	0	0	0	0
		LARGE	Construc.	8	3	5	16	0	1	17
			Construc.	8	3	5	**16**	**0**	**1**	**17**
		SMALL	WRT	33	36	109	177	0	4	151
		MEDIUM	WRT	7	9	23	39	0	1	39
		LARGE	WRT	54	102	130	286	0	4	158
			WRT	93	147	262	502	0	8	349
		SMALL	Transp.	0	0	20	20	0	5	55
		MEDIUM	Transp.	34	46	53	133	0	5	222
		LARGE	Transp.	5	21	24	50	0	16	137
			Transp.	39	68	96	203	0	25	414
		SMALL	FS&I	30	18	50	98	0	13	468
		MEDIUM	FS&I	9	139	632	780	0	0	7
		LARGE	FS&I	58	35	96	189	1	26	903
			FS&I	96	192	778	1.066	1	40	1.377
		SMALL	SCS	2	1	3	6	0	0	30
		MEDIUM	SCS	0	0	0	0	0	0	0
		LARGE	SCS	15	0	8	23	0	0	0
			SCS	16	1	11	29	0	0	30
		Intermediate	Dom. C.	1.236	607	2.417	4.261	5	131	6.832

Source: Author´s elaboration based on the IOM 2008 (CCNN-CDR; 2011).

INTERMEDIATE UTILIZATION BY SECTORS AND SIZE. (I)

M&Q	Manufacturing			MAN	EGW			EGW
3	23	6	1.571	1.600	0	0	16	16
1	3	1	386	389	0	0	4	4
6	67	191	2.668	2.926	0	0	27	27
10	**93**	**198**	**4.624**	**4.915**	**0**	**0**	**46**	**46**
1	2	0	8	10	0	0	0	0
0	0	0	97	98	0	0	1	1
1.978	14	12	1.310	1.336	1	0	21	22
1.980	**17**	**12**	**1.415**	**1.444**	**1**	**0**	**22**	**23**
4	107	45	54	206	0	0	1	1
1	12	86	73	172	0	0	1	1
1.479	465	611	4.039	5.115	47	30	636	713
1.484	584	742	4.167	5.494	47	**30**	**637**	**714**
0	0	0	2	2	263	0	371	634
0	0	0	1	1	0	171	240	411
1.232	57	46	1.087	1.190	0	0	2.772	2.772
1.232	57	46	1.090	1.193	263	171	3.383	3.817
0	0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0
18	7	7	62	76	6	4	71	80
18	**7**	**7**	**62**	**76**	**6**	**4**	**71**	**80**
155	81	72	403	555	3	2	43	48
40	19	18	102	138	1	0	9	10
162	123	99	610	832	4	2	52	58
357	**223**	**188**	**1.115**	**1.526**	**7**	**5**	**104**	**116**
60	26	5	229	260	0	0	5	5
227	88	58	885	1.031	1	0	17	18
153	22	47	239	308	11	7	147	165
439	136	110	1.353	1.599	12	**8**	**168**	**189**
482	108	84	962	1.154	0	0	83	83
7	63	24	192	279	1	1	14	16
929	208	162	1.857	2.226	0	0	160	160
1.418	379	270	3.011	3.660	1	1	257	258
30	4	5	104	113	1	1	19	22
0	0	3	0	3	0	0	0	0
0	18	0	119	138	0	0	1	1
31	22	8	224	254	1	1	20	23
6.968	1.518	1.582	17.061	20.160	338	219	4.709	5.267

Table 7.2. (A). Continued.

				INTERMEDIATE UTILIZATION BY SECTORES AND SIZE (III)										
				Financial and Insurance activities.			FIA	Social and Community Services		SCS	TIU	SME TIU	LSE TIU
Production	Domestic Production	**SMALL**	AFF	0	2	3	5	1	0	1	2	1.749	113	1.599
		MEDIUM	AFF	0	1	1	2	4	0	3	8	444	38	433
		LARGE	AFF	5	42	26	73	8	0	13	22	3.745	618	3.069
			AFF	**5**	**44**	**30**	**80**	**13**	**1**	**18**	**31**	**5.938**	**769**	**5.101**
		SMALL	M&Q	0	0	0	0	0	0	0	0	1.749	4	123
		MEDIUM	M&Q	0	0	0	0	0	0	0	0	444	1	99
		LARGE	M&Q	0	7	38	45	0	0	0	0	3.745	97	3.357
			M&Q	**0**	**7**	**39**	**46**	**0**	**0**	**0**	**0**	**5.938**	**102**	**3.579**
		SMALL	Manuf	1	2	6	9	11	1	31	43	1.749	299	189
		MEDIUM	Manuf	60	90	113	263	23	4	86	113	444	894	893
		LARGE	Manuf	146	117	390	654	111	19	555	684	3.745	4.352	7.543
			Manuf	**207**	**209**	**510**	**926**	**145**	**23**	**672**	**839**	**5.938**	**5.545**	**8.624**
		SMALL	EGW	0	0	3	4	0	0	0	0	1.749	264	3.819
		MEDIUM	EGW	0	0	2	2	0	0	0	0	444	171	247
		LARGE	EGW	53	76	167	296	38	14	395	447	3.745	686	5.641
			EGW	**53**	**77**	**172**	**303**	**38**	**14**	**395**	**447**	**5.938**	**1.121**	**9.707**
		SMALL	Construc.	0	0	0	0	0	0	0	0	1.749	0	344
		MEDIUM	Construc.	0	0	0	0	0	0	0	0	444	0	0
		LARGE	Construc.	28	58	66	152	32	8	1.235	1.274	3.745	313	1.456
			Construc.	28	**58**	**66**	**152**	**32**	**8**	**1.235**	**1.274**	**5.938**	**313**	**1.800**
		SMALL	WRT	32	26	77	135	28	8	165	202	1.749	723	1.071
		MEDIUM	WRT	24	7	51	82	14	11	51	77	444	214	716
		LARGE	WRT	85	62	205	353	44	20	140	204	3.745	1.431	1.391
			WRT	142	96	**332**	**570**	**86**	**40**	**356**	**482**	**5.938**	**2.368**	**3.179**
		SMALL	Transp.	4	12	43	59	3	0	1	3	1.749	625	1.885
		MEDIUM	Transp.	31	26	116	173	9	3	18	30	444	1.202	1.875
		LARGE	Transp.	182	33	389	604	36	12	271	320	3.745	645	1.969
			Transp.	217	71	548	**835**	**49**	**15**	**290**	**353**	**5.938**	**2.472**	**5.730**
		SMALL	FS&I	506	188	926	1.620	42	56	409	508	1.749	1.749	5.964
		MEDIUM	FS&I	195	206	379	780	58	25	263	346	444	1.520	2.811
		LARGE	FS&I	976	362	1.787	3.126	82	108	789	979	3.745	3.376	6.329
			FS&I	1.677	756	3.092	5.526	**182**	**189**	**1.462**	**1.833**	**5.938**	**6.645**	**15.104**
		SMALL	SCS	22	3	39	63	22	1	93	116	1.749	101	4.901
		MEDIUM	SCS	2	0	48	51	4	81	17	102	444	90	93
		LARGE	SCS	0	2	3	5	13	0	334	347	3.745	70	481
			SCS	24	5	90	119	39	82	444	565	5.938	262	5.476
		Intermediate Dom. C.		2.353	1.323	4.880	8.555	584	373	4.869	5.826	53.444	19.597	58.299

Table 7.2. (A). Continued.

INTERMEDIATE UTILIZATION BY SECTORS AND SIZE. (II)

SECTORSÇ				Construction			CONST	Wholesale and Retail Trade			WRT	Transport & Comunications			T&C
Production	Domestic Production	**SMALL**	AFF	0	0	0	0	9	1	37	46	0	4	0	4
		MEDIUM	AFF	0	0	0	0	26	3	10	38	0	1	0	1
		LARGE	AFF	1	1	2	3	51	5	66	121	0	7	0	8
			AFF	**1**	**1**	**2**	**3**	**85**	**8**	**112**	**206**	**1**	**12**	**0**	**13**
		SMALL	M&Q	0	0	0	0	0	0	0	0	0	0	0	0
		MEDIUM	M&Q	0	0	0	0	0	0	2	2	0	0	0	0
		LARGE	M&Q	18	13	53	84	0	0	29	29	0	3	0	4
			M&Q	**18**	**13**	**53**	**84**	**0**	**0**	**31**	**32**	**0**	**3**	**0**	**4**
		SMALL	Manuf	10	7	28	45	107	7	24	137	0	0	0	1
		MEDIUM	Manuf	10	7	28	45	72	14	92	178	4	5	13	22
		LARGE	Manuf	718	523	2.113	3.354	729	104	495	1.328	97	350	650	1.097
			Manuf	**737**	**537**	**2.169**	**3.444**	**908**	**125**	**610**	**1.643**	**101**	**355**	**663**	**1.120**
		SMALL	EGW	0	0	2	2	0	0	1	1	0	0	0	0
		MEDIUM	EGW	0	0	1	1	0	0	0	0	0	0	0	0
		LARGE	EGW	14	10	58	83	162	36	174	372	57	13	107	176
			EGW	**14**	**10**	**62**	**86**	**162**	**36**	**175**	**373**	**57**	**13**	**107**	**176**
		SMALL	Construc.	0	0	0	0	0	0	0	0	0	0	0	0
		MEDIUM	Construc.	0	0	0	0	0	0	0	0	0	0	0	0
		LARGE	Construc.	2	2	7	11	60	20	72	152	58	11	44	113
			Construc.	2	**2**	**7**	**11**	**60**	**20**	**72**	**152**	**58**	**11**	**44**	**113**
		SMALL	WRT	88	64	258	410	120	16	83	220	10	100	100	210
		MEDIUM	WRT	17	13	51	81	32	5	26	63	3	33	19	55
		LARGE	WRT	102	74	301	477	352	65	376	793	48	190	319	557
			WRT	207	151	**609**	**968**	**504**	**86**	**486**	**1.076**	**60**	**323**	**438**	**822**
		SMALL	Transp.	0	0	0	0	173	34	243	450	223	140	322	685
		MEDIUM	Transp.	14	10	41	65	481	93	658	1.232	15	288	63	366
		LARGE	Transp.	20	15	62	97	93	22	123	238	61	41	1.554	1.656
			Transp.	34	25	103	**162**	**747**	**149**	**1.024**	**1.920**	**299**	**468**	**1.939**	**2.706**
		SMALL	FS&I	0	0	470	470	393	80	496	969	100	131	357	588
		MEDIUM	FS&I	47	34	137	218	498	120	473	1.091	72	29	127	228
		LARGE	FS&I	0	0	907	907	758	154	957	1.869	194	252	689	1.134
			FS&I	47	34	1.515	1.596	**1.648**	**354**	**1.926**	**3.929**	**366**	**412**	**1.173**	**1.950**
		SMALL	SCS	2	2	6	10	25	7	19	51	2	3	3	7
		MEDIUM	SCS	0	0	0	0	0	0	2	2	0	0	13	14
		LARGE	SCS	0	0	0	0	9	2	15	26	10	0	0	11
			SCS	2	2	6	10	34	9	36	79	12	3	16	32
		Intermediate Dom. C.		1.063	775	4.528	6.365	4.150	786	4.473	9.409	954	1.600	4.381	6.935

Table 7.2. (B). Matrix of Inter-Sectorial and Size Relationships of the Chilean Economy. Imported Intermediate Consumption.

			Agriculture, forestry and fishing				AFF	Mining and quarrying			M&Q	Manufacturing			MAN	EGW			EGW	Construction
			SECTOR / SIZE	S	M	L	AFF	S	M	L	M&Q	S	M	L	MAN	S	M	L	EGW	S
PRODUCTION	Imported Production	SMALL	Agric	2	0	0	2	0	0	0	0	0	1	0	1	0	0	0	0	0
		MEDIUM	Agric	0	0	0	0	0	0	0	0	0	0	5	5	0	0	0	0	0
		LARGE	Agric	89	1	43	134	0	0	0	0	25	156	230	410	0	0	2	2	0
		Total	AGRIC	92	1	43	136	0	0	0	0	26	156	234	416	0	0	2	2	0
		SMALL	M&Q	0	0	0	0	0	2	0	2	4	1	107	112	25	16	324	365	0
		MEDIUM	M&Q	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
		LARGE	M&Q	0	2	13	15	0	0	202	203	20	11	3.912	3.942	18	11	264	293	2
		Total	M&Q	0	2	13	15	0	2	203	205	24	11	4.019	4.054	43	28	587	658	2
		SMALL	Manuf	13	0	6	19	0	0	1	1	194	46	159	399	0	0	2	2	9
		MEDIUM	Manuf	78	0	1	79	0	0	0	0	10	29	9	48	0	0	0	0	3
		LARGE	Manuf	74	201	436	711	1	22	1.160	1.184	257	431	4.251	4.940	59	38	792	889	305
		Total	Manuf	164	202	442	809	1	22	1.162	1.186	461	506	4.420	5.387	59	38	795	891	317
		SMALL	EGW	0	0	0	0	0	0	0	0	0	0	0	0	2	1	25	28	0
		MEDIUM	EGW	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
		LARGE	EGW	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
		Total	EGW	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
		SMALL	WRT	0	1	1	3	0	3	18	20	3	3	212	217	0	0	2	2	0
		MEDIUM	WRT	0	1	1	3	0	3	18	20	3	3	212	217	0	0	2	2	0
		LARGE	WRT	0	0	1	1	0	0	0	0	0	1	13	15	0	0	0	0	0
		Total	WRT	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
		SMALL	T & C.	0	0	0	0	0	0	0	0	0	1	6	8	0	0	0	0	0
		MEDIUM	T & C.	0	0	1	1	0	0	0	0	0	2	20	22	0	0	0	0	0
		LARGE	T & C.	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
		Total	T&C	0	0	3	3	0	2	95	97	16	3	179	198	7	5	91	102	2
		SMALL	FIA	0	0	3	3	0	2	95	97	16	3	180	199	7	5	91	102	2
		MEDIUM	FIA	0	0	0	0	0	0	0	0	0	0	1	1	0	0	0	0	0
		LARGE	FIA	0	0	0	0	0	0	0	0	1	0	5	6	0	0	0	0	0
		Total	FIA	0	0	0	0	0	0	0	0	1	0	5	6	0	0	0	0	0
		SMALL	SCS	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
		MEDIUM	SCS	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
		LARGE	SCS	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
		Total	SCS	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
		INTERMEDIATE IMPORTED CONSUMPTION		256	207	504	967	2	30	1.478	1.509	530	682	9.090	10.302	110	72	1.502	1.684	322

Source: Author´s elaboration based on the IOM 2008 (CCNN-CDR; 2011).

		CONST	Wholesale and Retail Trade			WRT	Transport & Comunications			T&C	Financial and Insurance activities.			FIA	Social and Community Services			SCS	Total Intermediate Imported Utilization	TIIU	TIIU
M	L	CONST	S	M	L	WRT	S	M	L	T&C	S	M	L	FIA	S	M	L	SSC		MSME	LSE
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	3	3	0
0	0	0	4	0	0	4	0	0	0	0	0	0	0	0	0	0	0	1	10	4	6
0	0	0	3	0	8	11	0	1	0	1	1	8	13	21	1	0	1	2	582	285	297
0	0	0	7	1	8	15	0	1	0	1	1	8	13	22	1	0	2	3	595	293	303
0	2	2	0	0	3	3	0	0	0	0	0	1	3	4	0	0	0	0	490	49	440
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
1	7	11	0	0	89	89	1	10	0	10	0	6	13	19	0	0	0	0	4.581	81	4.500
1	9	13	0	0	93	93	1	10	0	11	0	6	16	22	0	0	0	0	5.071	130	4.940
6	26	41	22	2	12	36	0	0	2	3	2	2	8	12	8	0	7	16	529	306	223
2	10	16	8	2	10	20	2	1	18	20	14	2	27	43	6	1	14	22	248	159	89
222	902	1.429	267	50	380	698	75	775	1.465	2.315	161	162	428	751	58	17	410	485	13.403	3.178	10.225
231	938	1.486	298	54	402	754	78	776	1.485	2.338	177	167	462	805	72	18		90	13.748	3.643	10.537
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	29	3	26
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0	12	12	0	0	1	1	0	0	7	7	20	0	20
0	0	0	0	0	0	0	0	0	4	4	0	0	0	0	0	0	0	0	5	4	46
0	0	0	8	2	16	26	0	1	0	1	0	1	2	2	0	0	1	1	273	21	252
0	0	0	8	2	16	26	0	1	16	18	0	1	3	3	0	0	9	9	298	22	277
0	1	1	6	1	11	18	9	23	551	583	0	2	26	27	0	0	0	0	645	42	603
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	3	3	3	85	1.131
0	1	1	0	0	5	5	12	0	915	927	0	2	42	44	0	0	11	11	996	16	980
0	1	1	6	1	17	24	21	24	1.466	1.510	0	4	67	72	0	0	14	14	1.645	58	1.586
0	0	0	0	0	0	0	1	0	45	46	0	0	2	2	0	0	9	9	58	1	57
2	7	11	54	13	72	139	24	1	142	167	222	21	374	617	2	1	46	49	1.383	75	2.623
2	7	11	54	13	72	140	24	1	187	212	222	22	376	619	2	2	55	58	1.441	375	1.065
0	0	0	0	0	1	2	1	0	68	69	0	0	14	14	0	19	1	20	106	22	85
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	3	3	9	1	8
0	0	0	0	0	2	2	1	0	68	69	0	0	14	14	0	19	3	23	115	398	1.158
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
234	956	1.512	373	71	610	1.054	125	812	3.222	4.159	400	208	950	1.558	76	39	598	198	22.942	4.922	19.892

Table 7.2. (C). Matrix of Inter-Sectorial and Size Relationships of the Chilean Economy. Final Utilization.

			FINAL UTILIZATIÓN									
Total Domestic Intermediate Utilization	Sectors	Size	Government	Low Income Households	Medium Income Households	High Income Households	Non Profit Private Org.	Changes in inventories	Gross Fixed Capital Formation	Exports	Toral Final Utilization	GVP
1.749	AFF	S		50,7	54,5	73,9		25,8	33,8	24,4	263,0	2.011,8
444	AFF	M		54,7	58,9	79,8		1,5	124,0	944,4	1.263,3	1.707,3
3.745	AFF	L	17,5	149,2	160,6	217,6		-124,7	97,3	210,8	728,4	4.473,9
5.938	AFF	Total	17,5	254,6	274,1	371,3	0,0	-97,4	255,0	1.179,7	2.254,8	8.193,0
12	M&Q	S		0,1	0,1	0,2		0,4		0,0	0,8	13,1
102	M&Q	M						25,5		312,5	338,0	440,1
3.534	M&Q	L						-114,9		16.911,4	16.796,5	20.330,4
3.648	M&Q	Total	0,0	0,1	0,1	0,2	0,0	-89,0	0,0	17.223,9	17.135,3	20.783,6
455	Manuf	S	11,5	490,7	646,3	1.182,9		7,3	17,6	249,5	2.605,7	3.060,5
1.868	Manuf	M	2,5	179,2	236,0	432,0		58,3	65,6	97,8	1.071,4	2.939,1
15.020	Manuf	L	34,4	1.311,7	1.727,4	3.161,9		811,7	705,7	12.179,2	19.932,0	34.952,0
17.342	Manuf	Total	48,4	1.981,6	2.609,6	4.776,8	0,0	877,3	788,9	12.526,5	23.609,1	40.951,5
643	EGW	S									0,0	642,8
416	EGW	M									0,0	416,5
6.665	EGW	L	35,4	461,2	493,4	764,2					1.754,2	8.419,2
7.724	EGW	Total	35,4	461,2	493,4	764,2	0,0	0,0	0,0	0,0	1.754,2	9.478,5
0	Construc.	S							3.170,7		3.170,7	3.170,7
0	Construc.	M							2.311,2		2.311,2	2.311,2
1.893	Construc.	L							7.418,5		7.418,5	9.311,1
1.893	Construc.	Total	0,0	0,0	0,0	0,0	0,0	0,0	12.900,4	0,0	12.900,4	14.793,0

Table 7.2. (C). Continued.

			FINAL UTILIZATIÓN									
Total Domestic Intermediate Utilization	Sectors	Size	Government	Low Income Households	Medium Income Households	High Income Households	Non Profit Private Org.	Changes in inventories	Gross Fixed Capital Formation	Exports	Total Final Utilization	GVP
2.112	WRT	S	163,8	740,1	1.116,8	2.943,0	0,0	3,4	677,0	472,7	6.116,8	8.228,7
585	WRT	M	0,0	130,1	191,8	481,3	0,0	0,7	132,2	85,1	1.021,2	1.606,5
3.721	WRT	L	0,0	670,7	949,0	2.169,4	0,0	4,0	794,6	908,0	5.495,8	9.217,3
6.419	WRT	Total	163,8	1.541,0	2.257,6	5.593,6	0,0	8,2	1.603,8	1.465,8	12.633,8	19.052,5
1.541	Transp.	S		107,2	163,0	329,6				435,0	1.034,8	2.575,9
3.275	Transp.	M		2,7	4,2	8,4				203,3	218,7	3.493,4
3.591	Transp.	L		856,8	1.302,5	2.634,3				3.309,3	8.103,0	11.694,1
8.407	Transp.	Total	0,0	966,8	1.469,7	2.972,4	0,0	0,0	0,0	3.947,6	9.356,5	17.763,4
5.970	FS&I	S	35,0	72,6	149,0	1.335,0			318,1	239,5	2.149,2	8.119,7
3.745	FS&I	M	58,8	19,5	40,1	359,3			69,6	21,6	569,0	4.313,8
11.520	FS&I	L	67,6	140,1	287,4	2.575,9			613,7	462,2	4.147,0	15.667,3
21.236	FS&I	Total	161,5	232,3	476,5	4.270,2	0,0	0,0	1.001,4	723,3	6.865,2	28.100,8
417	SCS	S	90,6	203,0	336,6	959,2	717,1	3,1			2.309,6	2.726,8
172	SCS	M	14,3	79,1	131,1	373,6				9,2	607,2	778,8
551	SCS	L	9.964,1	1.305,5	2.164,5	6.168,4		0,0	-150,2	952,4	20.404,6	20.955,9
1.140	SCS	Total	10.068,9	1.587,6	2.632,2	7.501,1	717,1	3,1	-150,2	961,6	23.321,4	24.461,5
73.747			10.495,4	7.025,2	10.213,1	26.249,9	717,1	702,2	16.399,3	38.028,4	109.830,6	183.577,8

Source: Author´s elaboration based on the IOM 2008 (CCNN-CDR; 2011).

Using first information from the table (7.2.A.), we can see that the 183,578 billion of intermediate consumption and value added, that made part of the GVP, 73.747 billion are the utilization of domestically produced inputs. From that amount, 54,150 billion (73%) corresponds to goods and services produced by means of utilization of domestically produced inputs by the strata of large companies, while Micro, Small and Middle-sized enterprises as a whole, produce goods and services by means of utilization of domestically produced inputs by only 19.597 billion (27%).

Focusing our attention only on the imported inputs (at Table 7.2 B), in which is recorded imported intermediate utilisation) we can see that total goods and services produced by means of imported inputs utilisation (23,372 billion) constitute 13% of total GVP and, within that figure, 18.825 billion (81% of utilization of domestically produced inputs) are utilised by large enterprises, whereas SME utilise only 19% of imported inputs (4,547 billion).

The Large-Scale firms of Mining and Manufacturing sectors utilise 19,521 billion in imported inputs, a figure that is equivalent to 66% of the total imported inputs utilised by the economy, and to 82% of imported inputs utilised by all the large enterprises (18.827 billion).
Each one of the remaining sectors have a low component of imported inputs within its intermediate consumption and giving a disaggregated mind looking at the figures of the two major users of imported inputs, we will see that in the mining sector 97% of this consumption is concentrated in large enterprises, while 71% of the intermediate consumption of the manufacturing sector is also concentrated in large enterprises.

Within Total Intermediate Utilisation (97.121 billion), 73,747 billion (76%) corresponds to production based on national inputs and 23,374 (24%) based on imported inputs, then we can conclude that the production´s composition of the leading export sectors of the Chilean economy cannot be considered compatible with a strategy of modernisation, innovation and self-sustainability.

Despite the full openness of the Chilean economy, only two sectors reported a significant weight on the use of imported inputs; manufacturing and mining. Each of the remaining sectors possesses one very less weight of imported inputs within its intermediate consumption. Moreover, intermediate consumption is concentrated in large companies in the mining sector, as well as large companies in the manufacturing sector.

When we look forward, the detail of the intermediate consumption analysing their participation in value added of the economy, we can see from another perspective that in the mining and manufacturing sectors, the total value of imported inputs of large scale firms (18,826 billion) are equivalent to 90% of the total added value produced by the large-scale firms of both sectors (20.823 billion), as can be visualised in Tables 7.2. A and 7.2.B.

Additionally, from already presented Tables 7.1.A and 7.1.B, we can see that, in 2008, within the Chilean Gross Value of Production (GVP) of 183,578 billion pesos, there is a value added of 86,457 billion (47 % of GVP). That value includes 1,520 billion in general taxes and 1,445 in other taxes (in total 1.6% of GVP). Also, incorporated into the figure are 49,359 billion in operating surplus or capital remuneration (26.9% of GVP) and 34,133 billion in wages (18.6% of GVP).

A preliminary conclusion that can be extracted from both pairs of figures (7.1 and 7.2) is quite clear. The impact of the opening has not spread to the business fabric. There no evidence supporting the neoliberal forecasts of a big absorption of technology from abroad in all firm´s sizes and sectors of the economy exposed to global commerce.

The only sectors that are absorbed imported inputs in a significant proportion are mining and manufacturing. In both cases that pattern of intermediate utilization is limited to obtain inputs, at low international prices, and "proprietary technologies" coming from matrix houses to domestic subsidiary firms, showing very weak backward and forward linkages with the rest of the economy.

The trade openness gains promised by neoliberal, should have a direct expression in patterns of final goods utilization produced in the Chilean economy, but as you will see in Tables 7.2. (C) which describes the structure of Final Utilization of GVP, the impact of these gains over these patterns is not clear at all. From the demand side, this table registers 109,831 billion in Final Utilisation (60% of GVP); 10,495 billion corresponds to Government Consumption, 43,488 billion to Household´s Consumption, 717 billion to Non-Profit Private Organisations' Consumption, 702 billion to Changes in Inventories, 16,399 billion to Gross Investment in Fixed Capital and 38,028 billion to inputs used by the Export Sector. The Chilean households register a Final Utilisation value of 43.488 billion; 16.2% of it corresponds to low income household consumption (40% of households), 23.5% corresponds to medium income household consumption (30% of households) and 60.4% of high-income household consumption (30% of

households). This distribution makes it evident that the final households´ consumption is highly concentrated in high-income sectors and this segment is being provided with goods and services produced by LSE.

The substantial market power of larger Chilean companies lets them controls without restriction both Intermediate Consumption and Final Demand of the economy. At an aggregate level, the segment of LSE supply to SME 11,588 billion (48% total utilization of domestic inputs) and demand from small and middle-sized firms 15,498 billion (29% of their intermediate demand), remaining 71% of its demand is provided by firms of their own size.

Additionally, LSE's control the bulk of domestic demand coming from households (39% of GVP) and from the Government (5.7% of GVP). Moreover, Government Consumption is even more concentrated than Household Consumption, a tendency that has been growing from 1990 onwards.

The external sector is supplied as well by large enterprises which provide it 34,933 billions of final goods and services (92% of final demand of exporter sector).

Notwithstanding, neoliberal forecasts, this sector tend to be highly concentrated and there no evidence of promised tendency to diversification of firms oriented to supplying exporters acting as indirect exporters. After forty years of full opening, clearly Chilean economy continues waiting for the emergence of that ensured virtuous circle.

In short, the undeniable market power of large Chilean business groups, as well as their dominant position in the leading sectors of the Chilean economy is highly related to their control of the intermediate inputs supply and of their simultaneous control of final demand. However, now for this research would be necessary understand which kind of institutional arrangements are inducing that kind of market control.

In our opinion would be necessary analyse that point focus our attention on the institutions of governance, but that is not an approach frequently used in the Chilean discussions.

The dominant neoliberal point of view (e.g. Cuddington et al 2002) argues that in cases such as the Chilean one, this kind of outcomes (high market´s concentration, hyper-primary specialization and elimination of SME from the markets) must be

considered in agreement to the expected ones. From this point of view, these supply and demand arrangements only would reflect the difference in productivities, between sectors and among sizes of enterprises, induced by the trade openness. It would be only producing an appropriate specialization of the economy and a purge inefficient firms operating in the markets.

If this arrangement, as has happen in the Chilean case, led to a specialization in primary industries and in low value-added commodities, neoliberals argue that as a consequence of that Chile would face a stream of high value-added input and output production, coming from the manufacturing sector of developed countries. Those final goods and intermediate inputs would have embodied a high level of technical progress, which would exceed the level of technical progress embodied on the primary and backward manufacturing sector of non-developed countries. In these cases, they argue that the supply of manufactures of more developed countries (MDC), would grow faster than the supply of commodities from less developed counties (LDC). The results would be a decline in the relative supply of commodities that, in turn, would induce a shift in the equilibrium, producing an increase in the relative price of primary commodities. This relative price change would constitute an improvement in the terms of the trade of LDC commodity exporters, because technical progress in industrialised countries would be translated into welfare gains for developing countries. Unfortunately, those virtuous circumstances only occur occasionally at world markets, and seem far from constituting a general rule, at least in the Chilean case, in which the described behaviour has not occurred. On the contrary, the more possible scenario is not of markets returning to a balance of prices which results, in not very long periods, by adjusting supply and demand on both sides of the trade relationship. The scenario that would ends up settling, in the mid-long term, tends to be one of consolidation in terms of trade extremely asymmetric and unequal.[248]

In the area of technological absorption is clear that Chilean copper mining companies maintain a high dependency on Australian, American and Canadian inputs and technology (a situation which explain the high level of imported inputs consumption).

248 In the Chilean case, after a long cycle of high price commodities, induced by the growth of the Chinese economy, the price`s progression seems to have collapsed, due to at least three causes: 1) The lack of demand for raw materials (once China´s growth decreased). 2) The excess of commodities supply, induced by their high profitability, a tendency that has operated in exactly the opposite direction to the predictions of the neoliberal hypothesis. 3) The low capabilities of Chilean economy to absorb technical progress in their primary and secondary sectors. Independently which, primary prices evolution resembles to forecast made by neoliberals, the Chilean strategy of development has had incorrect results.

That situation is not a consequence of evolution of relative prices but of institutional arrangements that promote it. In fact, are the business models of large foreign mining companies who promote vertical integration as an easy way to send to their headquarters profits which avoid paying domestic taxes. By this way, that strategy contributes to encapsulate technical progress of mining sector, isolating them to the rest of Chilean economy.

The other leading export sector, Chilean paper and cellulose industry, continues dependence on New Zealand technology, and when the price of any sectorial inputs of that origin increase and the output prices fall, the most common scenario is the erosion of sectorial profitability and, as is happening currently, it will have a recessive impact on the economy as a whole.

Table 7.3. Composition and Sectorial Distribution of Value Added and GVP of Chilean Economy.

Componentes of Value Added and GVP (absolute values)	AFF	M&Q	MAN	EGA	CONST	WRT	TR	FIA	SCS	TOTAL
Total Intermediate Consume	5.228	8.477	30.462	6.951	7.877	10.463	11.095	10.113	6.456	97.121
Taxes	10	1	18	1	9	24	411	530	516	1.520
Other Taxes	78	18	158	6	106	334	-81	253	573	1.445
Operating surplus	1.589	10.760	6.490	2.201	3.534	3.563	4.127	10.359	6.736	49.359
Labour Remunerations	1.289	1.527	3.823	319	3.268	4.668	2.211	6.847	10.181	34.133
Total Value Added	2.966	12.306	10.489	2.527	6.917	8.589	6.668	17.989	18.006	86.457
Gross Value of Production	8.193	20.784	40.952	9.478	14.793	19.052	17.763	28.101	24.462	183.578

Componentes of Value Added and GVP (Share)	AFF	M&Q	MAN	EGA	CONST	WRT	TR	FIA	SCS	TOTAL
		M&Q	MAN	EGA	CONST	WRT	TR	FIA	SCS	
Taxes	0,01%	0,00%	0,01%	0,00%	0,00%	0,01%	0,22%	0,29%	0,28%	0,83%
Other Taxes	0,04%	0,01%	0,09%	0,00%	0,06%	0,18%	-0,04%	0,14%	0,31%	0,79%
Operating surplus	0,87%	5,86%	3,54%	1,20%	1,93%	1,94%	2,25%	5,64%	3,67%	26,89%
Labour Remunerations	0,70%	0,83%	2,08%	0,17%	1,78%	2,54%	1,20%	3,73%	5,55%	18,59%
Total Value Added	1,62%	6,70%	5,71%	1,38%	3,77%	4,68%	3,63%	9,80%	9,81%	47,10%
Gross Value of Production	4,46%	11,32%	22,31%	5,16%	8,06%	10,38%	9,68%	15,31%	13,33%	100,00%

Source: Author´s elaboration based on the IOM 2008 (CCNN-CDR; 2011).

This situation, which is repeated in most of the sectors of the economy with a specialization in primary products, has led to, as shown forward in the matrix of added value (Table 7.3. or bottom side of 7.1 matrixes) that reported below how the value added of the economy is unevenly distributed between sectors, generating extremely high returns to the capital (operating surplus) in the financial and services sectors, secondarily in mining and manufacturing sectors and lower returns in the remaining sectors.

7.10. The Structural Matrix of Chilean Economy

In the already displayed tables 7.1; 7.2 and 7.3, we developed an analysis focused on the sectorial characteristics of the relationships established between different kinds of firms operating in several sectors of the economy. Now, from another perspective, in Tables 7.4 (A), 7.4 (B) and 7.4 (C), we present three different versions of a stylized structural matrix of the Chilean economy that exclude sectorial relationship analysis. We develop there a complementary analysis focused only the relationship established between different sizes of firms, an exercise that makes clearest the characteristics of Chilean economic governance. Using the methodology described previously, we obtained now an even more stylised Structural Economic Matrix (SEM) of the Chilean Economy for year 2008.[249] This new matrix here presented (7.4. (A)), included a record of the economic relations between firm size´s strata disaggregated as before (Tables 7.2).

7.11. Size Structure and Intermediate Consumption

In Table 7.4. (A), SEM lets us evaluate the influence that each size of firm has on the production levels of the economy. It also allows us to evaluate the influence of each size of firm on the final utilisation of goods and services.

249 This matrix, in sum, is a sectorial aggregation and a size disaggregation of IOM information recorded on Tables 7.1.and a consolidation by sizes of IOM information recorded on Tables 7.2.

Table 7.4. (A). Structural Economic Matrix of the Chilean Economy (SEM) disaggregated by size (In current billions of Chilean pesos 2008)

		Intermediate Utilization				Final Utilization	
Components of GVP	Firms / Size	Small	Medium	Large	Total	Government	Low Income Households
	Small	2.685	1.192	9.022	12.899	301	1.664
	Medium	2.458	1.673	6.476	10.607	76	465
Domestic Production	Large	7.057	4.531	38.653	50.241	10.119	4.895
	Total DP	12.200	7.397	54.150	73.747	10.495	7.025
Imports	Total M	2.193	2.354	18.827	23.374	0	949
	General Taxes	241	108	1.170	1.520		
	Other Taxes	280	211	954	1.445		
	Operating surplus	7.871	4.910	36.578	49.359		
Value Added	Labour Remunerations	7.765	3.026	23.342	34.133		
GVP		30.550	18.007	135.021	183.578		

Source: Author´s elaboration based on the IOM 2008 (CCNN-CDR; 2011).

	Medium Income Households	High Income Households	Non Profit Private Org.	Changes in inventories	Gross Fixed Capital Formation	Exports	Total FU	Total
	2.466	6.824	717	40	4.217	1.421	17.651	30.550
	662	1.734	0	86	2.703	1.674	7.400	18.007
	7.085	17.692	0	576	9.480	34.933	84.780	135.021
	10.213	26.250	717	702	16.399	38.028	109.830	183.578
	1.526	4.358	481	6.062	925	0	0	37.675

Using this tool, it is possible to visualise the role that each size of companies contributes to the intermediate consumption of each size of company, identifying the role of each stratum as a provider of its own inputs and those used by the remaining size strata. We can also observe the orientation of the final demand of the families of different income levels and the final demand from other actors. In both cases, we can observe in a disaggregated way, the final utilisation of products supplied by each size strata of firm to their final recipients (Chilean government, households, exporting sector and others).

From Table 7.4. (A), firstly, we can observe the orientation of final demand of the families of different income levels and, secondly, the statuses of final demand from other actors. In relation to households, we proceeded to disaggregate intermediate utilisation in function of the destination of their outputs, visualising the origin (by size) of items in which households spend their incomes.

From there we will able to visualize whether trade openness has exerted a positive influence on the economy as a whole, or if its impact is only concentrated in some sectors or firm sizes. Doing so, we can better visualise the real impact of trade openness strategy on relationships among firms of different sizes, as well as determining whether trade openness has allowed the Chilean economy to overcome pre-existing technological heterogeneity between Small, medium and large enterprises.

The data on Table 7.4 (A) shows production in its vertical axis and utilisation in its horizontal axis. From there, we can see that from the 183,578 billion forming the GVP utilised in 2008, 135,021 billion corresponded to inputs, goods and services produced by large companies, whilst micro, small and middle-sized enterprises produced, in aggregate, only 48,557 billion.[250] We can also see at this matrix that whilst Small businesses utilise 2,193 billion of total imported inputs, middle-sized firms use 2,354 billion and large enterprises utilise 18,827 billion. The data on Table 7.3 (A) shows production in its vertical axis and utilisation in its horizontal axis. From there, we can

250 As referred to above, in 2008 sales of large companies constituted 86% of the total sales of the economy. For this reason, we should assume that their VBP possesses a higher level of added value, and its participation in the GDP should be higher. However, as the column of inventory variations reveals, the value of this in the case of MSME is 126 billion, whilst in large companies it is only 576 billion. As the GDP is equal to the sum of the Value Added and the Intermediate Consumption, and Gross Value of Production is equal to Sales value less inventory variation, the large variation of inventories existing in large companies generates a greater difference between Sales and the GVP. It is for this reason that Sales of large companies, still 86% of total sales, only contributes 74% to GDP.

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These figures show that in the enterprises of larger size, they use a mix of inputs with an imported component, in absolute and relative terms, much higher relatively than that of their smaller sized peers. From the 183,578 billion that comprised the GVP in 2008, 135.021 billion corresponded to goods and services produced by the strata of large companies, whilst micro, small and middle-sized enterprises produced, in total, only 48.557 billion.[252]

These relationships mainly confirm general tendencies already described in other chapters and that were estimated from different sources. However, establish the nature of outcomes emerging from specific arrangements that define characteristic of business model predominating in Chilean economy, made necessary a more detailed analysis that require visualize Table 7.4 (B), in which SEM is presented disaggregated by size of firm´s strata, but with final and intermediate utilisation, as well as value added, represented as vertical percentages of GVP.

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252 From this table, it is possible also to visualize the weight of exports in the Chilean economy as a whole. Exports, as shown in the matrix of Final Utilization, are 38,028 billion, while Intermediate Utilization of domestic inputs reaching 73,747 billion and imports to 23,374 billion. As you can observe, these figures exports play a secondary role in the GVP of 183.578 billion and also within the value added (GDP) that ascend to 86,457 billion. If compared with imports (23,374 billion), we see that you overcome these in a 63%, generating a significant surplus in the balance of trade (which declined significantly in the coming years), a fact which has an undoubted positive effect; however we see that the Chilean economy continues concentrated in domestic markets of non-tradable goods produced by larger enterprises, while their exports have low added value, are extremely concentrated in commodities highly sensitive to variations in international prices of these and are mainly produced by larger firms (84,780 billion).

When percentages are expressed in a vertical way, we can visualise total utilisation in the final row, and their origin in each column (e.g. intermediate utilisation of resources by each size of enterprise and of final utilisation in any of eight types of final demand), in each respective square of each intermediate row. The use of SEM expressed in percentages of GVP, allowed us to visualize the participation of different size companies in the total intermediate inputs and final products utilisation (domestic and imported) estimated as a proportion of total supply and demand. That means that we can visualise, because of such information, which size of firms produce the goods and services, in which the utilisation is focused; the magnitudes and proportions in which production and utilization area distributed and, additionally, we can observe the influence that intermediate and final demand exerts on the aggregate supply produced by companies of every size and productivity level.

From Table 7.4 (B), it is possible to see that domestic inputs production is equivalent to 40.2% of GVP. Utilization of imported inputs ascend to 12.7% and value added to 47.1% of GVP.

Table 7.4. (B). 2008 Structural Economic Matrix of the Chilean Economy (SEM) disaggregated by size. (In vertical percentages)

		Intermediate Utilization				Final Utilization									
Components of GVP	Firms / Size	Small	Medium	Large	Total	Government	Low Income Households	Medium Income Households	High Income Households	Non Profit Private Org.	Changes in inventories	Gross Fixed Capital Formation	Exports	Total	GVP
Domestic Origin Production	Small	8,8%	6,6%	6,7%	7,0%	2,9%	23,7%	24,1%	26,0%	100,0%	5,7%	25,7%	3,7%	16,1%	16,6%
	Medium	8,0%	9,3%	4,8%	5,8%	0,7%	6,6%	6,5%	6,6%	0,0%	12,2%	16,5%	4,4%	6,7%	9,8%
	Large	23,1%	25,2%	28,6%	27,4%	96,4%	69,7%	69,4%	67,4%	0,0%	82,0%	57,8%	91,9%	77,2%	73,5%
	Domestic Inputs	39,9%	41,1%	40,1%	40,2%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%
Imported Inputs	Imported inputs	7,2%	13,1%	13,9%	12,7%										
Total Production		47,1%	54,2%	54,0%	52,9%										
	Taxes	0,8%	0,6%	0,9%	0,8%										
	Subsidies	0,9%	1,2%	0,7%	0,8%										
	Operating surplus	25,8%	27,3%	27,1%	26,9%										
	Labour Remunerations	25,4%	16,8%	17,3%	18,6%										
Value Added	Total Value Added	52,9%	45,8%	46,0%	47,1%										
Gross Value of Production		100%	100%	100%	100%										

Source: Author´s elaboration based on the IOM 2008 (CCNN-CDR; 2011).

In addition, we will use Table 7.4 (C), in which SEM is also presented disaggregated by size of firm´s strata, but with final and intermediate utilisation, as well as value added, represented as horizontal percentages of GVP. When percentages are expressed in a horizontal way, we can visualise total utilisation in the final column, and the destiny of the product of each row (e.g. Small, Medium or Large firms), that means, intermediate utilisation of resources by each size of enterprise and final utilisation in any of eight types of final demand.

From Table 7.4 (C), it is possible to see that domestic inputs production are utilized practically in the same proportion (around 40% of their respective contribution to GDP) by the three sizes of enterprises. On the other hand, in the medium and large enterprises, utilization of imported inputs fluctuates around 13% of their respective contribution to GDP, but in the small enterprises, utilization of imported inputs is only around 7% of that contribution.

Table 7.4. (C). Structural Economic Matrix of the Chilean Economy 2008 (SEM) disaggregated by size. (In horizontal percentages).

		Intermediate Utilization				Final Utilization									
Components of GVP	Firms / Size	Small	Medium	Large	Total	Government	Low Income Households	Medium Income Households	High Income Households	Non Profit Private Org.	Changes in inventories	Gross Fixed Capital Formation	Exports	Total	GVP
	Small	8,79%	3,90%	29,53%	42%	1,0%	5,4%	8,1%	22,3%	2,3%	0,1%	13,8%	4,7%	57,8%	100,0%
	Medium	13,65%	9,29%	35,96%	59%	0,4%	2,6%	3,7%	9,6%	0,0%	0,5%	15,0%	9,3%	41,1%	100,0%
	Large	5,23%	3,36%	28,63%	37%	7,5%	3,6%	5,2%	13,1%	0,0%	0,4%	7,0%	25,9%	62,8%	100,0%
	Intermediate Domestic Inputs	6,65%	4,03%	29,50%	40%	5,7%	3,8%	5,6%	14,3%	0,4%	0,4%	8,9%	20,7%	59,8%	100%
	Intermediate Imported Inputs	5,82%	6,25%	49,97%	62%										
Production	Total Intermediate Production	14,82%	10,04%	75,14%	100%										
	Taxes	15,85%	7,13%	77,01%	100%										
	Subsidies	19,37%	14,63%	66,00%	100%										
	Operating surplus	15,95%	9,95%	74,11%	100%										
	Labour Remunerations	22,75%	8,86%	68,38%	100%										
Value Added	Total Value Added	18,69%	9,55%	71,76%	100%										
Gross Value of Production		16,64%	9,81%	73,55%	100%										

Source: Author´s elaboration based on the IOM 2008 (CCNN-CDR; 2011).

If we focus our attention only in demand side (e.g., domestic input consumption) described at Figure 7.4 (D), where the different components of intermediate utilization (segmented by size´s origin) are estimated as a proportion of total domestic intermediate utilization, the situation look even more clear.

Table 7.4. (D). Composition of Intermediate Utilization Disaggregated by size. (As a percentage of Intermediate Utilization).

Components of GVP	Firms / Size	Intermediate Utilization			
		Small	Medium	Large	Total
	Small	3,6%	1,6%	12,2%	17,5%
	Medium	3,3%	2,3%	8,8%	14,4%
	Large	9,6%	6,1%	52,4%	68,1%
Domestic Production	Intermediate Utilization of Domestic Inputs	16,5%	10,0%	73,4%	100,0%

Source: Author´s elaboration based on the IOM 2008 (CCNN-CDR; 2011).

Considering MSME as a combined group, we can observe that 11% of total domestic intermediate utilization (TDIU) correspond to utilization of inputs demanded by small and medium firm and supplied by others small and medium firms. On the other hand, LSE demand 52% of total domestic inputs utilised in the economy from others LSE but at the same time production process, acting as the "best client" of smaller firms (demanding 21% of TDIU) and the best provide, delivering to small and medium enterprises, inputs equivalents to 18% of TDIU of the Chile´s economy.

All that means which, there is a level of input´s self-supply between firms that is inversely proportional to firm´s size, a situation that is clearly displayed at this Table, in which the same figures formerly exposed as percentages of GVP, now are expressed as percentage of Total Intermediate Utilization (TIU).

If we give a look to the same figures from the supply side or from the demand side, the general tendency of dominance of LSE remain constant and their market control is overwhelming, both when operating as customers, and when they do as suppliers.

7.12. Size Structure and Final Utilisation

We have already analysed how, at the level of Intermediate Production, both production of domestic inputs and utilization and of such inputs, are dominated by LSE. However, at the level of final utilisation of gods and services, as it is presented at the sub-tables displayed at Tables 7.5.A, 7.5.B, 7.5.C and 7.5.C, the situation is even more problematic, because the bulk of final demand of all institutional sectors, is massively satisfied by larger firms and only a reduced proportion by small and middle-sized firms.

Figures about Final Utilisation are reported at Tables 7.5 (A) in CH$ of 2008 and in Figures (B); (C) and (D) figures are displayed in different kinds of percentages.

Table 7.5. (A). Composition of Final Utilisation of Goods and Services (In billions of CH$ 2008)

Final Utilization									
Government	Low Income Households	Medium Income Households	High Income Households	Non Profit Private Org.	Changes in inventories	Gross Fixed Capital Formation	Exports	Total FU	GVP = IU + FU
301	1.664	2.466	6.824	717	40	4.217	1.421	17.651	30.550
76	465	662	1.734	0	86	2.703	1.674	7.400	18.007
10.119	4.895	7.085	17.692	0	576	9.480	34.933	84.780	135.021
10.495	7.025	10.213	26.250	717	702	16.399	38.028	109.830	183.578

Source: Author´s elaboration based on the IOM 2008 (CCNN-CDR; 2011).

Figure 7.5 (A) display situation of the institutional sectors that demand final products. They are displayed in a disaggregated level, showing be extremely segmented. A high proportion of Total Final Utilisation (TFU) of goods and services in the economy (109,830 billion) is concentrated in two sectors, "High Income Households" and the "Exporter Sector". This Table, also shows that the others sources of final utilisation of domestic products are: "Government", with a F.U. of 10,495 billion, (9.6% of F.U.) and "Gross Fixed Capital Formation", with 16,399 billion (14.9% of F.U), "Low Income Households" with 7,025billion (6.4% of F.U.) and Medium Incomes Households with 10,213 billion (9.3% of F.U.), are the remaining segments of utilisation.

Table 7.5. (B). Composition of Final Utilisation of Goods and Services by Size of Firms as a Percentage of Total Final Utilization)

		Final Utilization								
		Government	Low Income Households	Medium Income Households	High Income Households	Non Profit Private Org.	Changes in inventories	Gross Fixed Capital Formation	Exports	TotalFinal Utilization
Domestic Origin Production	Small	0,27%	1,52%	2,25%	6,21%	0,65%	0,04%	3,84%	1,29%	16,1%
	Medium	0,07%	0,42%	0,60%	1,58%	0,00%	0,08%	2,46%	1,52%	6,7%
	Large	9,21%	4,46%	6,45%	16,11%	0,00%	0,52%	8,63%	31,81%	77,2%
	Total DIU	9,56%	6,40%	9,30%	23,90%	0,65%	0,64%	14,93%	34,62%	100,0%

Source: Author´s elaboration based on the IOM 2008 (CCNN-CDR; 2011).

Figure 7.5 (B) display the same figures expressed as percentages of Total Final Utilization. "High Income Households" represent 23.9% of TFU and the "Exporter Sector" 34.6% of TFU), in total 60% of TFU of the economy. This Table also shows that the others sources of final utilisation of domestic products are: "Government" (9.6% of F.U.) and "Gross Fixed Capital Formation" (14.9% of F.U), "Low Income Households" (6.4% of F.U.) and Medium Incomes Households (9.3% of F.U.). Those institutional sectors demand and utilise products which are supplied in a high proportion by LSE (48% of total F.U.) and in reduced proportion by SME (11% of total F.U.).

The sectors of minor importance accumulate final demand in a fragmented way and oriented to final products provided by LSE, which supply 77% of the demand for final goods displayed by the Chilean economy yet.

Concentration of demand is explained by the fact that, the main sectors behave in a way favourable to that, showing the hard presence of factors that condition that conduct. For instance, households being disaggregated by income level, show that, regardless of their level of income (low, middle or high, it spends most of their expenditure on goods and services produced by sectors of larger size. LSE are providers of 69.7% of goods consumed by households of low-incomes, 69.4% of the goods used by middle-incomes households and 67.4% of goods consumed by high-income households.

Table 7.5. (C). Composition of Final Utilisation of Goods and Services (as horizontal Percentage of Total Final Utilization)

		Final Utilization								
		Government	Low Income Households	Medium Income Households	High Income Households	Non Profit Private Org.	Changes in inventories	Gross Fixed Capital Formation	Exports	TotalFinal Utilization
Domestic Origin Production	Small	1,70%	9,43%	13,97%	38,66%	4,06%	0,23%	23,89%	8,05%	100,0%
	Medium	1,02%	6,29%	8,95%	23,44%	0,00%	1,16%	36,52%	22,62%	100,0%
	Large	11,94%	5,77%	8,36%	20,87%	0,00%	0,68%	11,18%	41,20%	100,0%
	Total DIU	9,6%	6,4%	9,3%	23,9%	0,7%	0,6%	14,9%	34,6%	100,0%

Source: Author´s elaboration based on the IOM 2008 (CCNN-CDR; 2011)

Looking at the same figures from the perspective of utilisation (e.g. who consume supplied goods), Table 7.5. (C) provide additional information. 6% of production of large companies' production is utilised to fulfil "Low Income Households" demand; 8% of its production to fulfil "Medium Income Households" demand and 21% of its production to fulfil "High Income Household Demand". LSE does not register delivery of final goods to "Non-Profit Private Organizations", who are supplied basically by small firms. However, middle-sized enterprises utilise 6% of their production to fulfil "Low Income Households" demand, 9% of its production to fulfil "Medium Income Households" demand and 23 % of its production to fulfil "High Income Household" demand. In turn, Small enterprises utilise 9% of their production to fulfil "Low Income Households" demand, 14% of its production to fulfil "Medium Income Households" demand and 39% of its production to fulfil "High Income Household" demand

Table 7.5. (D). Composition of Final Utilisation of Goods and Services (as Vertical Percentage of Total Final Utilization)

		Final Utilization								
		Government	Low Income Households	Medium Income Households	High Income Households	Non Profit Private Org.	Changes in inventories	Gross Fixed Capital Formation	Exports	Total
Domestic Origin Production	Small	2,87%	23,69%	24,15%	26,00%	100,00%	5,71%	25,72%	3,74%	16,1%
	Medium	0,72%	6,63%	6,48%	6,61%	0,00%	12,25%	16,48%	4,40%	6,7%
	Large	96,41%	69,68%	69,37%	67,40%	0,00%	82,05%	57,81%	91,86%	77,2%
	Total DIU	100,0%	100,0%	100,0%	100,0%	100,0%	100,0%	100,0%	100,0%	100,0%

Source: Author´s elaboration based on the IOM 2008 (CCNN-CDR; 2011).

As we can see at Figure 7.5.D, there is a constant tendency in the distribution of goods supplied by each size of company to households of different income levels. But, in average around 77% of the final demand of each institutional sector (not only higher income household's demand) is oriented towards final goods produced by larger enterprises. A more detailed perspective of final demand composition is also revealed in this Table.

There not greater differences on the percentage of final demand, of each strata of household, supplied by LSE. However, there are large differences in the orientation of the production of each size of companies to each stratum of household. The participation of each size of enterprises in the provision of domestic goods demanded by each category of final utilisation from a vertical perspective. From this Table, we can observe that 96% of government utilisation and 92% of export utilisation are supplied by large enterprises. In addition, 82% of goods that are used to change inventories and 58% of goods utilised in the gross fixed capital formation are produced by large enterprises.

This last situation is particularly remarkable: Small and medium firms are providing 42% of gross fixed capital formation with domestic goods, and from those goods, 42% are produced by SME reflecting that these strata remain an important player in the area of fixed investment. However, LSE supply 57.8% of this demand. The normal arrangements to this respect are characterized by important presence of subcontracts by means which LSE organize chain of SME in order to attend segments of demand controlled by them but which don lets them to use their "scale economies". However, the general tendency is an increment in vertical integration and a reduction of market share of SME suppliers of Capital Goods (IRS, 2016).

This tendency of raising LSE control of Final demand is spreading on all sectors of the Chilean productive fabric. On the one hand, the participation of small and middle-sized enterprises (SME) represents in total only 8% of domestic goods utilised by export activities. However, and given the structure of final demand, when the country increases its exports, the economy will demand only 8% of goods required for the production of its exports that came from small and middle-sized firms, but 92% of such goods will come from larger enterprises.

All firms utilise an extremely reduced amount of intermediate inputs produced by small firms and middle-sized enterprises and even them, utilize a small proportion of inputs produced by firms of their own size. In turn, larger firms utilise a large proportion of

intermediate inputs produced by firms of their own size, and only a reduced amount of inputs produced by small and middle-sized enterprises.

The implications of this situation are quite clear. Given the current conditions of low-productivity and productive disarticulation between sizes of companies, even though MSME explains about 70% of total employment in the economy, contribute little to the growth process of the national economy. This occurs because large companies mainly demand inputs from companies of a similar productivity. However, when small and middle-sized companies require inputs, they also do so from LSE.

The first conclusion that it is possible to draw from these figures, is that the Chilean economy is subject to high levels of vertical integration mixed with an even greater concentration by size of firms. The ten thousand big corporations that the Chilean IRS defined as Large Enterprises, had in 2008, sectorial market shares exceeding the worldwide concentration standards accepted by antitrust authorities, moreover, their global market share were, this year, about 70% of total sales of the economy.[253] Additionally they provide almost 74% of inputs produced by the economy. They are also the main input suppliers of the about 740 thousand companies that Chilean IRS defines as SME. This data confirms the lack of integration within the economy which particularly affects low-productivity and middle-sized companies.

We have displayed abundant information that makes clear the lack of density of the Chilean productive fabric, a situation that is reflected in the absence of functional inter-sectorial and synergic inter-size and intra chains relationships. This lack of appropriate linkages generates a weak articulation of the intermediate production of different sizes of firms, reducing to a minimum the forward and backward linkage that would allow small and middle-sized enterprises to be reinforced by the productive activities of larger firms. On the contrary, given the absence of any counterweight at markets absolutely controlled by the larger companies, the severe absorption of intermediate demand from large enterprises has occurred, excluding small and medium firms from the inputs markets

In an open economy, every company should be able to import inputs from abroad, replacing those, which the domestic market offers at inconvenient prices, or that are

253 The LSE market share reported by Chilean IRS in 2008 was over 80% but about 10% of these figures correspond to state owned companies and others independent firm, for that reason we estimate the real market share of LSE controlled by larger business group in only 70%.

of poor quality. However, Chilean importation of inputs appears concentrated in large firms (80%) and small-sized firms appear increasingly dominated by extremely concentrated larger domestic goods suppliers.

Then, these issues raised two relevant questions that this research needs to answer:

- What kind of arrangements has concentrated al that level supply and demand for inputs in so few companies?
- Which rules of the game govern the Chilean economy that have made it possible that trade openness not stimulate the diversification of input supply, which would enable better dissemination of technological progress and an expansion of the market share of the smaller and medium companies?

Answering those two questions requires analysing the specific mechanisms through which situation has been installed

The information already displayed show that even though the Chilean economy is already fully open, the effects of openness that are channelled through the final demand are solidly linked to large companies. This group, at the same time as succeeding in connecting to some segments of the international markets 'demand, by means of a set of arrangements mainly developed during the post dictatorship period.

The above institutional arrangements define characteristics of interactions among Micro, Small and Middle-sized Firms (MSME) with Large Scale Enterprises (LSE), but their implementation is additionally oriented to a kind of "market skimp" given that these powerful firms prefer to establish close relationships only with a small group of MSME hierarchically organized.

LSE organize clusters of MSME around a large buyer firms, in a kind of hierarchical relationships that substitute market relationships by vertical practices of coordination, a situation that generally involve a hard subordination of smaller firms and the labour force to the business interests of LSE (Ossandon y Tironi, 2013).

These new neoliberal hierarchized business relationships are not only based in the eight kinds of arrangements already described. These are just the main institutional arrangements whose practical operation define leading characteristics of the framework in which the neoliberal institutions of governance have been built. However, the goals of these institutions are not reduction or elimination of small-scale firms costs

of transaction, on the contrary, their purposes are oriented to reduce or eliminate any potential competitive advantages of smaller firms and expand markets power of large-scale companies.

The outcomes of the Chilean model are dependent on the neo-liberal institutional environment, but mainly on the institutional arrangements built between 1990 and 2009. These were based on the political decisions of new authorities and constituted an essential part of the institutional framework within which the Chilean economy operates (Undurraga, 2012). As was mentioned in previous chapters, those arrangements have resulted in important levels of economic concentration, and reciprocally, in a drastic fall of the percentage participation of MSME in the GDP, the value of total exports, the volume of sales, and in the level of employment produced by MSME.

In short, the use of some mechanisms as the outlined above, have formed a dense institutional fabric, which has cut potential connections among the international demand and non-traditional exports. Control of the export sector´s intermediate demand, as well as control of domestic markets of final imported goods, has been placed in the hands of large companies, expelling smaller companies from them.

On that bases, the large companies have designed and installed the grounds of the market governance of domestic input demand. In a few words, they administer foreign demand for exportable goods; the internal demand for inputs incorporated within Chilean exports; the substitutes for domestic demand of some imported gods and the domination of imported goods market, a key area that may be visualized looking at the bulk of the contribution to GVP, made by the wholesale and retail trade sector. All of this information forms a clear picture of the way in which LSE have taken control of the main part of Chilean foreign trade, internal markets and other areas of the domestic economy like government consumption. Even when trade openness endorses export and import activities as a possibility which, theoretically, is open to companies of all sizes, in reality this does not occur. The control of foreign trade by large companies, exerted by means of the control of intermediate consumption and final demand, has almost completely inoculated small companies (and to the country) against the multiples positive effects that trade liberalisation could offer them.

The already analysed figures clearly demonstrate this. Large-scale firms are in some degree oriented towards foreign trade especially toward commodities markets, however 75% of LSE never have exported. On the other hand, SME are mainly oriented to

domestic markets. In 2009, 50% of exporting firms sold less than USD$100,000 in foreign markets, and the total value of exported goods by small firms barely surpassed 1% of the total exports from Chile.

This is an issue worth highlighting because the productive convergence proposal, stimulated by supporters of trade opening, assumes that all export sectors will develop strong linkages between sectors and company sizes, so that openness would act as a mechanism to spread technical progress and modernisation to the economy as a whole. However, in the Chilean case, we note that when combining a highly regressive income distribution with a structure of weak linkages between sectors and companies, followed by implementation of a predatory business model, trade openness and market liberalization can hardly generate, by themselves, productive convergence in the Chilean economy and its benefits tend to be concentrated in a few large economic actors.

If we analyse only the features of household's final destination, a sector that consumes 40% of final goods and services, we can see that this is an area in which main economic relationships are not those established between firms, but between consumers and firms- that is a fact that must be stressed.

Objective deployment of positive outcomes associated with trade openness and market liberalisation, seem to be conditioned to the presence of adequate connections between the consumption of high-income households and the different sizes of firms. However, that connections are very different to those existing in the Chilean economy at the firm level. In that area, large-sized companies end up imposing consumption patterns highly exclusionary of participation of other segments of firms.

Within that context, LSE are able to enforce their capital accumulation process, but at the same time are structurally unable to promote and disseminate technical progress in the economy. In a nutshell, the institutional environment and the institutional arrangements which define Chilean consumption patterns are in such way overlapped, that they have become a sort of "market-trap" that constrain economic growth, establish hard boundaries to progressive income redistribution, even though it favours market power amplification of dominant business groups.

7.13. Size Structure of Added Value

From a perspective of IOM analysis, economic theory tells us that heterogeneity observed at the level of intermediate relationships and final demand will be expressed in the areas of wages and capital remunerations (Keuning and de Ruuter, 1988, Keuning, 1991). With this in mind, we decided to concentrate our efforts on discovering in what proportion the value added to the Chilean economy by each segment of firms, corresponded to labour remunerations or capital retributions and which are the variables that condition that distribution.

We have already mapped the situation of intermediate and final utilisation, now we will obtain an initial approximation of the process of income distribution, observing the form in which added value is distributed between capital, labour and taxes paid to government. Based on this, we analyse the payments to labour and capital factors in Tables 7.6. (A), (B), (C) and (D), in order to evaluate if the bulk of payments to both factors are actually focused on LSE, in the same way that intermediate consumption and final destination is.

Table 7.6. (A). Value Added of the Chilean Economy: Disaggregation by Size of Firm.

Components of GVP	Firms Size	Components of VA			
		Small	Medium	Large	Total
	General Taxes	241	108	1.170	1.520
	Other Taxes	280	211	954	1.445
	Operating surplus	7.871	4.910	36.578	49.359
Value Added	Labour Remunerations	7.765	3.026	23.342	34.133
Total Value Added (VA)		16.157	8.256	62.044	86.457

Source: Author´s elaboration based on the IOM 2008 (CCNN-CDR; 2011).

Tables 7.6 (A) and 7.6 (B), shows us that, Total Value Added of the economy (86,457 billion), is 47% of GVP (183,578 billion); within that amount, 49.359 billion CH$ corresponds to Operating Surplus (27%); 34,133 (40%) to Labour Remunerations and 2,965 (1.6 %) to different kind of taxes. However, distribution of VA is very asymmetrical.

Table 7.6. (B). Value Added Disaggregated by Size of Firms as percentage of VA of the Chilean Economy.

Components of GVP	Firms Size	Components of VA as % of total VA			
		Small	Medium	Large	Total
		0,28%	0,13%	1,35%	1,76%
		0,32%	0,24%	1,10%	1,67%
		9,10%	5,68%	42,31%	57,09%
Value Added		8,98%	3,50%	27,00%	39,48%
Total Value Added		18,69%	9,55%	71,76%	100%

Source: Author´s elaboration based on the IOM 2008 (CCNN-CDR; 2011).

From Table 7.6. (B), is also clear that the absolute value of the payments to the workers, for the sum of small and middle-size enterprises, 10,791 billion CH$, (12,5% of VA) is less than a half of 23,342 billion wages pay by LSE (27% of VA).

Next Table 7.6. (C) shows that, if we visualise former information from other perspective, in horizontal percentages of total value added.

Table 7.6. (C). Matrix of Inter-Sectorial and Size Relationships of the Chilean Economy. Value Added Disaggregation by Size. (In horizontal percentages)

Components of GVP	Firms Size	Components of VA as % of VA (horizontal)			
		Small	Medium	Large	Total
	General Taxes	15,85%	7,13%	77,01%	100,00%
	Other Taxes	19,37%	14,63%	66,00%	100,00%
	Operating surplus	15,95%	9,95%	74,11%	100,00%
Value Added	Labour Remunerations	22,75%	8,86%	68,38%	100,00%
Total Value Added		18,7%	9,5%	71,8%	100%

Source: Author´s elaboration based on the IOM 2008 (CCNN-CDR; 2011)

This figure let us see that, in the case of small firms, their operating surplus is equivalent to 16% of the total operating surplus of the economy, incorporated in value added. In the case of middle-sized firms, it is 10% of the total operating surplus of the economy, incorporated in value add and lastly, in the case of large firms; it is also 68% of operating surplus that made part of the added value of the economy. On the other hand, in the smaller firms, labour remunerations are 23% of the total value of

compensations incorporated in value added, 9 % in the case of middle-sized firms and 68% in the case of LSE.

Table 7.6. (D). Matrix of Inter-Sectorial and Size Relationships of the Chilean Economy. Value Added Disaggregation by Size. (In vertical percentages)

Components of GVP	Firms Size	Components of VA as % of VA (vertical)			
		Small	Medium	Large	Total
	General Taxes	1,49%	1,31%	1,89%	1,76%
	Other Taxes	1,73%	2,56%	1,54%	1,67%
	Operating surplus	48,72%	59,47%	58,96%	57,09%
Value Added	Labour Remunerations	48,06%	36,65%	37,62%	39,48%
Total Value Added		100%	100%	100%	100%

Source: Author´s elaboration based on the IOM 2008 (CCNN-CDR; 2011).

Contrariwise, if these figures are observed vertically (Table 7.6 (D)), it is possible to observe that, while small companies divide their added value almost equally between capital and labour (49% and 48%), in medium-sized companies, while the value of the operating surplus it is 59%, the remunerations to work amount to only 37%. The same happens in the case of the LSE whose figures are 59% and 38% respectively.

Differences existing between LSE and MSE, between labour remuneration and capital operating surplus, may be explained by the presence of economics rents captured by the LSE, which are produced due the presence of mayor differences between the already analysed gap between labour remuneration, and labour productivity evolution. Another possible explanation is that, additionally, returns to capital coming from LSE underpay labour, is being complemented by rents associated to LSE negative business treatment towards the SME.

In both cases these situations (underpay wages and predatory business relationships) are impossible to be sustained without the presence of formal arrangements established between labour and capital, whether they were voluntarily accepted, or if are imposed by the intervention of some authority.

Any attempt to undermine the legal foundations of such institutional arrangements (stab which, have been quite scarce post 1990), generally is presented by neoliberals as

an attack on property rights, an erosion of the empire of law and like an undermining of the basic institutions that ensure economic progress.

That is a point of view which tends to be applauded by the multilateral financing agencies, and by some scholars who recognize rows within NEGT approach[254] (and by a few rational-choice institutionalists[255]. However, we believe that the dark picture they describe, in general is not adequate.

The actions, that for some constitute a threat to the institutional bases that are declared necessary for the progress of the economy, from another perspective are defined as adequate to implement the most relevant challenges that the Chilean economy needs to surpass the regressive relation established in Chile by the neoliberal model.
The relationship among weak, missing or perverse institutional arrangements and poverty, inequality and resource degradation. (Knack and Keefer, 1995; Rodrik, 2002).

7.14. Conclusions

The findings of our research displayed in the chapter shows the nature of relationships established among the main types of companies that constitute the Chilean economy. One group is composed by large firms that rule the markets and the other one includes a large group of SME subordinated enterprises, which maintain fragile and unequal linkages with large firms, with government and with high income households. The LSE drives the economy, defines the institutional arrangements that regulate their relationships with the rest of the economy and at the same time has meaningful power to define the core aspect of the institutional environment of Chilean society. On the other hand, the second, group, due to its small size and decreasing market share, has

254 Property rights institutions, which include protections against expropriation by the government, and contracting institutions, which facilitate private contracts between citizens, are evaluated by Acemoglu and Johnson (2001) as the essential institutions for development. They find that, when property rights institutions protect people from expropriation (for example, via high taxes, price controls, or outright confiscation), individuals can profit from investment in both physical and human capital. This investment produces higher rates of growth, which eventually yield much higher living standards.

255 Rational choice theory tends to view political institutions as structures of voluntary cooperation that resolve collective action problems and benefit all concerned, within that framework they assume that the incentive structure that exists when property rights are robust, and contracts are respected is the best scenery for development. That approach asses that, when property rights are weakened, economic growth is sacrificed, and human flourishing is constrained (Schmitz; 2006).

little impact on growth, despite and even has certain relevance demanding a large extent of total employment, is largely subordinated to characteristic of the institutional arrange installed y LSE and enforced from the State.

Supporting in facts this conclusion, the chapter let us conclude that:

- In the Chilean context, LSE, more than seek to engage in a multitude of market linkages with a large number of MSME, within a competition framework, primarily operate giving priority to the construction of networks of contractual relationships only with a few smaller firms. LSE establish with them hierarchical modalities of vertical integration. The institutions of governance who regulate economic relationship among different size of firms are who define occurrence of that situations in such a way that within that process. The role of small business, and labour force, partially or completely, are defined by LSE, utilizing their strong market power and rules of the game enforced by neoliberal regulations and by administrative actions implemented from the State, since 1990 forwards.
- LSE has conformed specific institutions of governance that allows them to expand their control over the markets and over MSME. The current strategy made possible by the former described market arrangements, consist on firing a growing group of its old suppliers of smaller size, replacing for production coming from companies of their own or by SME that run under their control based on hierarchical business arrangements, oriented to reduce the market share of the MSME.
- These predatory practices characterize the overriding business model of the Chilean economy. The set of institutional arrangements that are part of the "neo-liberal package", within which the institutions of governance of the Chilean markets are contained, have defined the character of this development model, ordering the economic activity as a whole. However, the power of the business model that made part of market´s institutions of governance, has installed a comprehensive set of recursive actions carried out by different actors. Those have given a unique cultural style, extremely competitive and individualistic, to Chilean society.
- The institutional arrangements contained within the leading business model have not presented as outcomes neither higher efficiency, nor reduction of transaction costs or improving of productivity. When looking at distribution of the value added, vis a vis evolution of the TFP in the Chilean economy, it seems clear that those arrangements are not running to maximize efficiency or

reduce transaction costs. To be more precise, they are only oriented to capture growing proportions of value-added but not to generate productivity.

- The performance productivity and efficiency of the companies is positively correlated with the level of cooperation and confidence between their members (workers and owners) and within their business network (LSE-MSME). The presence of bigger or smaller levels of productivity and efficiency in a high measure are function of those two variables (cooperation and confidence) both enforced by current institutional arrangements. If relations of unilateral power and highly hierarquical relationship induce interactions based on dependency and subordination, the lack of cooperation and confidence will tend to produce sub optimal levels of efficiency. That issue must be a good micro-explanation about an important part of reduced allocation efficiency of Chilean economy acting in a contrary sense to the effects of trade openness and liberalization influence on relative prices system.
- Disaggregation of IOM show that LSE are using a business model characterized by high vertical integration. This model organizes multiples institutional arrangements oriented to establish a hierarchy of relationship among different sizes of firms. As a consequence, the bulk of inputs used in domestic production by LSE and their own contribution to the intermediate production are mostly destined to be provided to companies of their same size. Moreover, large companies additionally demand the body of domestic input production and the greater part of the inputs imported by the economy. Given these figures, it is clear that large companies, controlled in turn by a small number of economic groups, have overwhelming control of both supply and demand for inputs in the economy. This results in their undeniable control of intermediate domestic production.
- Small and middle-sized companies have been losing control of the input market and continually diminishing their market shares. In the field of final demand, the situation is analogous, as corporations provide the bulk of domestic production of final goods and this amount includes the provision of majority of high-income household demand, practically all Government demand and much more than a half of the demand coming from the export sector.
- The soaring LSE market share (in inputs and final goods´ markets) iteratively exert its influence over the set of unequal rules of the game already installed but improved from 1990 forwards. The arrangements (of micro and macroeconomic order) made form to the arena within which smaller companies should compete. The asymmetric relationship that conforms that arena has produced a situation

in which, the MSME maintenance becomes critical. Furthermore, in tandem with the functioning of governance institutions biased against the MSME, has been produced further market power for the LSE. Such kind of power mainly rest the political and cultural influence of neoliberalism in Chile. In combination with other factors it has crystallised into a business model, which, step by step, increases the concentration of markets in a seemingly automatic way.

- The LSE' market power constitutes a powerful force in support of the neoliberal status-quo given that any development strategy, ignoring the aforementioned truths, even if it is oriented to obtain good distributional results, would certainly face setbacks in terms of economic growth.
- The description of the structure of the Chilean economy that the IOM presents when disaggregated by size, permits us to clearly observe how some of the most important automatic mechanisms, which are the basis for the permanence of neoliberal development model, operate. The performance of the Chilean LSE is related with two core factors, their control of processes of entrance and exit from the market and with the institutional arrangements established with other firms and agencies. In such a way, large firms have established a specific system of institutional governance operating against the competition rules and that handle several devices that provide solid and broad walls between them and the open market.
- Those devices allow larger enterprises to take competitive advantages over other sizes of firms, by means of the control of intermediate consumption and final demand. These controls are grounded inn a complex fabric of political and institutional factor and, all of them are supported by a sophisticated network of informal arrangements that literature define as "non-market activities". These activities have been intensified during four decades of market liberalisation and trade openness, allowing the serious capture of the political system and public policies.
- The narrowing of market share of smaller firms, by the action of larger economic groups, only has lost some degree of vigour as a result of the presence of external shocks, which have shrunk the aggregate demand and prevented its progression. However, the Chilean economy does not show greater signs of a reversal in its tendencies towards concentration.
- The different sizes of Chilean firms are linked in a differentiated way to domestic intermediate demand, which is produced by large companies and geared toward products and services produced by companies of similar size,

productivity and economically linked to the same business group or its partners. This situation is drive by a sophisticated set of formal and informal arrangements in which are involved large enterprises oriented to the domestic market, but also large companies operating in the export sector.

- The control of final demand is in the hands of large companies is based on their great capacity to shape the trade preferences of the public and make use of their tight control over their small suppliers, which are trying to capture the reduced market share that is not vertically integrated yet. The application of an aggressive and predatory business model, complemented by absolute control of the media and the publicity channels in the hands of a few large business groups, has resulted in their growing control of commercialisation channels. The hard rules of the game imposed by LSE that control these channels, has also been consolidated in specific institutional arrangements that make-up the LSE business model and define features of the Chilean market´s institutions of governance, as a whole.
- This situation is present sector-by-sector, independent of their specificities, in such a way that the patterns of Government consumption and also of Chilean families are highly conditioned by power of large companies. The LSE policy of vertical integration has promoted the well-known aggressive process of mergers and acquisitions. It constitutes an expression of certain previously negotiated business group alliances (domestic and global) and in general, constitutes a serious boundary to development of market competition.
- The vertical integration of LSE is generally built on business model, whereby some firms extracted substantial, and abnormal, revenues from their suppliers. In Chilean markets, asymmetry of contracts between sizes of enterprises is expression of business arrangements that the laws of developed countries do not accept in any way: Then, generalized result is insolvency of small enterprises and the absorption of its market share by larger enterprises that concentrate thereby increasing market power. The SEM presented in this chapter, exposed in a clear way the intensity with which this phenomenon has grown in markets that produce final consumer goods and those who concentrate the intermediate consumption. Practices that make possible such levels of concentration, are not regulated or condemned by the weak Chilean antitrust law, a situation which constitutes a break in the allegedly based on competition institutional environment. That situation does not seem worrying to neoliberal economist and either has been seriously faced by any post-dictatorship Government.

- All the previously described elements are the forces that have produced the concentration of intermediate supply and demand for inputs and the final demand for goods in so few companies and are the matrix upon which are built the institutions of governance that are ruling the Chilean economy. These rules have not allowed trade liberalisation to stimulate economic diversification that would enable the dissemination of technological progress in the productive fabric and the expansion of the market share of the small companies.
- The simultaneous presence of a discourse that defends free market and competition and predominance of a business model that promotes concentration and oligopoly of markets, is at the core of Chilean neoliberal model. That concentration permits their control of production and consumption at all levels and their control of half of the employment generation and, also, the definition of the conditions of economic stability or instability, which could affect flows of foreign investment, risk-classification of the country and, of course, the political stability of any government.
- All of this element frame parts and mechanisms that form the institutional structure of the Chilean economy. The system of market governance predominant in Chile presents some distinctive characteristics with regard to ownership, control, and capital markets, which emphasise its neoliberal character. It has been supported in promises (but not in facts) of obtaining, throughout openness and market liberalisation, an economy characterised by widely dispersed ownership, liquid stock markets, low levels of inter-corporate cross-holdings and competitive markets. Nevertheless, the economic dynamic, after the twenty years analysed here by means of disaggregated IOM, suggest that, contrary to neoliberal forecasts, the Chilean economy is typified by its high levels of ownership concentration, capital markets which induce low levels of liquidity in weaker firms, and lastly by a high degree of inter-corporate cross-holdings.
- In general, it is assumed that the optimal governance system is a function of parameters such as the degree of development of markets, the quality of the institutions and the productivity at firm level (Williamson, 1991).[256] Nevertheless in this chapter, after analysing Chilean economic relationships between sectors and sizes enterprises, it is necessary to express serious doubts

256 Williamson (1991) analyses the governance modes, seen as the result of the search for gains through the choice of cost-minimising factors, basically as a function of transactional dimensions (asset specificity, uncertainty and frequency). In the light of the evidence gathered in our research, we conclude that this perspective is unsatisfactory.

about the quality of institutions available to enforce business deals, as well as about the real nature of contracts that firms must accept in a context of high market asymmetries and who are in the origin of their low productivity.

- As we analyse the relationship between governance and productive efficiency in the Chilean case, we find that the neoliberal governance of firms has been followed by lower labour productivity and higher input costs, and not by the positive outcomes promised by the neoliberal proposal, related to the good governance of firms. Moreover, our findings suggest that under neoliberal governance, firms do not necessarily acquire, as the literature maintains, higher equity returns, better operating performance, and higher firm´s value. Actually, features of the Chilean model generally display a wide majority of firms framed in a picture clearly opposite to that.
- However, in the Chilean case, in a short-term analysis of LSE profitability and capital returns are very positive. As we will analyse in the next chapter, large firms were mostly acquired at a very low price (if any) within a spurious process of privatisations, and nowadays are inserted in an export led model focused on high price commodities, abundant natural resources and weak environmental regulation. Obviously, in this highly extractive context, those firms feel themselves part of a sort of a "neoliberal economic paradise" that would preclude non-necessary improvements of productivity, high quality management or innovation activities.
- As we have displayed in this chapter, public policies, the economic framework, the institutional environment and governance institutions reinforce this situation. Additionally, business models supported by institutions and by a political highly vulnerable to the influence of economic powers, are another asset in favour of the neoliberal model. In this context, it is understandable that neoliberalism, as ideology, be linked to the economic interests and strategies of large business groups and continues defending the adequacy of their proposals, even if these efforts go against all available evidence.

Chapter 8

Neoliberal Development Strategies and Institutional Traps

In the previous chapter, we analyse the from the economic side the business relationships and institutional arrangements existent in the Chilean economy between companies of different sizes belonging to different productivity strata. Instead, the objective of this chapter is to describe and evaluate, from the political side, the bases of the concentration process, both at the level of the institutional environment as to the level of institutions of governance.

Here we emphasise the way in which the roots of these process were defined, at the level of the political constitution of the state and of the others macro and micro rules of the game that have cemented the increasing market and non-market power of Chilean business groups.

This Chapter also deals with the constitutive elements of such rules of the game, both economic as well political, that defines the possibilities and limitations of trade openness in terms of exerting influence on the economic development process implemented by Chile.

The process of economic concentration is here analysed by observing how it links to the process of institutional capture of Chilean governments by the economic elites and then, based on the previous analysis, we describe the restrictions that the Chilean institutions exert at the level of institutional environment and at the level off arrangements that determine feasibility to obtain the development goals that the country seeks to achieve.

As we have previously analysed, the conceptual framework that, in recent decades, guided the Chilean process of economic openness has been solidly anchored in a neoliberal take on the neoclassical approach, which the market is not understood as a particular rule of the game. In fact, neoliberals don't see institutions in general and market in particular as "humanly devised constraints that structure human interaction" (North, 1990) either as "systems of established and embedded social rules that structure social interactions" (Hodgson 2006). To the contrary, from the neoliberal point of

view, individuals and prices are defined regardless of the mode of organisation of the economy. This means that for them, the "fully-rational-homo-economics" are able to freely choose the type of the economic interchange system to which they want to incorporate. Then, from neoliberal perspective, the study of the institutions should not be an adequate device for the analysis of the performance of a pricing system for which the basic principles of neoclassical economic theory should be used. Our analysis perspective, however, has been very different.

Given that we have previously falsified the core of neoliberal forecasts, showing how the outcomes of their development model have been very different from those promised at the time, being far below not only of their statements, but also of those imagens that have allowed to them to generate recognition from various sectors so far, the neoliberal perspective, we will now focus on an alternative analysis to theirs, using an institutionalist perspective.

8.1. An Institutional View of the Chilean Model Set-up

Within neoclassical theory, all endogenous variables are explained as the logical consequences of self-interested rational choice, whereby one's choice may be limited by the similarly motivated rational choice of others through any activity in the market. This form of rationality involves the maximisation of an objective function while facing given constraints (Boland, 1979). That means that neoliberals understood markets from a kind of "ideological" paradigm (Kuhn, 1981) that guides a set of actions and practical policies (supposedly aimed at a certain end), whose role sometimes seems to be to vest rather than orient their real goals.

However, the Chilean experience seems to show how when the time arrives to implement a process of economic and social transformations of some magnitude, in practical terms, the neoliberal model understood that put into operation process of macroeconomic adjustments, trade openness and price-liberalisation is not enough. The central issue to them is to ensure the long-term sustainability of the rules of the game that enable neoliberal reforms, assuming that these changes and the market itself, become by themselves appropriate devices to consolidate new allocation and distributional mechanisms. Therefore, even though Hayek (2001b) insists on a vision that of the economic order as endowed with an autonomous evolution, the implementation of this model in Chile was far from leaning to predominance of market mechanisms.

In this respect, in the previous chapters, we have shown that in the Chilean case, the installation of those rules of the game that have shaped the institutional environment of the country, have determined the structure of the economic system that organises the relations between economic actors from the political sphere. The political system has operated in Chile as the dominant sphere of the "action arena" from which the new forms of capital accumulation that currently characterise the economy have been articulated. From that perspective, the rules of the game may be delineated only after a feasible and complete set of such rules has materialised, as occurred in Chile after 1990.

In the Chilean case, following Ostrom's proposal (Ostrom et al, op. cit.: 41-43), we have assumed that, during the analysed period (1990 to 2009), politics as action arena was constituted by the intersection of these possible sets of variables. This occurred in a way which allowed economic agents to define the explicit or implicit assumptions which they used during this period, and to define their relationships within the organisation of the economic activities and concerning the nature of the community within which the arena played a role.

From this perspective, we will show in this chapter which political institutions have had the ability to affect (although not define or determine completely) the whole economic structure of the country, constituting the place where the institutional arrangements, that gave shape to the governance of the Chilean model, have been structured. We also show in this chapter that, empirically speaking, such institutional arrangements are far from neutral or defined with the purpose to reduce transaction cost.

On the contrary. They have reflected the specific configuration of existing power in the period under analysis, a configuration that has dramatically affected the balance of power in Chilean society. In turn, that new balance has been the core variable that allowed the establishment of economic and political structures that have defined the uneven distribution of wealth and power among the different Chilean economic agents and social groups.

8.2. Exogenous and Endogenous Factors in the Consolidation of the Chilean Model of Development

Just as we did in chapter II, when we examined the installation of the neoliberal economic model in Chile, in this chapter we will detail by analysing its consolidation

after 1990 and how these rules of the game, despite the important influence of powerful external factors over them, should be considered as endogenously determined.

The neoliberal thinking has sustained that for developing economies such as Chile, keeping a pro-market orientation, defending property rights, achieving a certain macroeconomic balance and driving "institutional" macro reforms that are focused on the prominence of private property rights are alone sufficient to achieve install an economic development. In their discourse, no relevant space is given to any other policies or institutional changes that may be required to attain this objective.

This assessment complies with the fact that the Chilean model was the result of an imposition of certain domestic political. The incidence of exogenous factors, such as the academic and political weight of the school of Chicago in the 70s, or the role of multilateral agencies in the adoption of The Washington Consensus, in the 90s, were strong; however, their recipes could not have been imposed whether they would not have coincided with the perspective and interests of national actors. The creativity and autonomy of Chilean actors expressed the strength of endogenous determinants and for that reason; it was the variable that gave shape to the Chilean model, and to the consequences associated with its implementation.

At the political level, institutional arrangements and the institutional environment in which the outcomes of the model took shape can be associated with different periods and actors. The dictatorship determined the institutional environment within which the Chilean model was implemented. Thus, they defined the macro rules of the game, grouped under the umbrella of the 1980 Constitution,[257] as well as its

257 The Political Constitution of the Republic of Chile of 1980 is the constitutional text currently in force in Chile. After the coup of September 11 of 1973, not only was the 1925 Constitution suspended, but also, it was sought to create a new institutionally that, some ideologues of the dictatorship tried to assimilate to corporatist structures of Franco Spain and others, whose ideas finally prevailed, to institutions inspired in neoliberal principles. A commission, appointed by the dictatorship composed of renowned right-wing lawyers, undertook the task of creating a new constitution, drafting the initial draft. A "Council of State", of similar composition, discussed and introduced some modifications to that project between 1978 and 1980; Subsequent to the editing refined by these advisory bodies, the "Junta de Gobierno", controlled by Pinochet himself, also introduced some changes. The text was nominally submitted to the opinion of the public through a so-called "National Plebiscite of 1980", in which the "new constitution" was approved. This plebiscite has been and continues to be questioned, given the formal irregularities of its celebration (among other things, for example, the country was under state of siege, there were no electoral registers and the opposition was prevented from campaigning, since some public freedoms, such as meetings, freedom of expression and freedom of expression, were restricted.).

association with the so-called "authoritarian enclaves". Nevertheless, the installation of a new institutional environment and institutional arrangements associated with the implementation of the neoliberal model, were mostly, designed, consolidated and refined in the 90s, during the post-dictatorship governments, which is the period that we have analysed in this research.

The great institutional rule of the Chilean neoliberal model is the Constitution of 1980, which, as we will discuss in this chapter, is an "Economic Constitution", since in it are legally ordered structures and economic relations in which not just citizens are involved. Additionally, this type of constitution increasingly involves the State itself in its role of protagonist in the development of economic life (Prosser, 2014).

The rules of the game that the neoliberal constitution applied to the Chilean economy were defined by the balance of power and political strategies that had existed during the dictatorship, which strongly limited the possibility of a subsequent change to those rules. The reason for the barely altered institutional environment of the 70s can be related to the type of political regime that was able to impose this authoritarianism.

That regime is, even at the present, an attenuated form of "democracy" of neoliberal orientation. It is a system of "semi-sovereign" representative democracy (Hunneus, 2015), which resembles the liberal democracy only in its formal aspects.

From 1990 onwards, there is a broad spectrum of legally established political parties in Chile. A parliament operates and it is elected together with the President of the Republic by means of free elections. Additionally, complete freedom of the press theoretically exists. However, each one of these elements has been neutralised by mechanisms ad-hoc, which are directly oriented to distorting the expression of the popular will. Some of them are political, others are economic and others cultural.

The free press and independent media are only free and independent from the State. The most marked case of concentration occurs with newspapers of national circulation, which are controlled by 99% by two business groups; four business groups control almost all radios and five groups control the TV channels. Mostly these media act, in the politic and cultural area, as a protecting trench of the neoliberal institutions.

Although large sections of the population did not recognize its validity, the Constitution of 1980 entered into force on March 11, 1981, in a transitional regime and, fully, on March 11, 1990. Its original text contained 120 articles, with 29 transitory terms.

From the economic side, the asymmetries of power and assets´ resource ownership pre-existing in an economy like Chile since before the introduction of the trade openness process, was a determinant variable that explained the establishment of particular social institutions of neoliberal character. They were promoted by the most powerful social and economic actors and ended by installing (as a product of the bargaining between the Right-Wing Parties and the Social Democrat -Social Christian Coalition), a set of institutions in charge of re-enforcement of pre-established commitments to the particular rules of behaviour already designed and implemented by the military dictatorship.

Obviously, the business groups that account for 70% of GDP and control behind 90% of the media advertising; own a resource that allows them to control the agenda of the media and prevent the emergence of defiant new media of different orientation, which, for this reason, does not have the advertising necessary for self-financing. Without relevant challenging actors, they have not adversary within the process of conformation of public opinion which, has become complete dominated by these incumbent business groups

From the political side, several powerful devices are in motion in a way that has been resilient to mayor changes. One of them is the lack of democratisation of the right wing and their permanent resistance to any political openness. Another factor has been the "neo-liberalisation" of the left wing. On that basis, the biggest cultural change in the post-dictatorship period has been the weakening of societal spirit that allowed the defeat of the dictatorship. The most important expressions of this weakening have been the reduction of associative tendencies and the de-politicisation of society. In the new context, individual strategies are privileged over the collective ones, people are positioned as spectators rather than actors, there is a marked contrast between private and public interests, an increase in the pursuit of competition and material success, as well as the transformation of consumption into a source of social prestige.

At the already described context shows, it is very clear that TWC was not the proposal that acted as a "guide" to the post-dictatorship Chilean economic programme. In reality, the proposal was adopted given that was functional to policy strategies previously developed in the country. Starting from there, given the support from multilateral agencies, those strategies could be expressed in the action arena with a force that allowed them to assume, in a non-always visible way, political and economic hegemony of the post-dictatorship governments. The TWC granted them a global perspective,

allowing it to overcome the character of a domestic political proposal, a fact which turned out to be quite attractive to the economists and politicians who went on to defend such an option. The dominance of TWC guidelines within the policies of the post-dictatorship governments was a key element of the non-democratisation of the right wing (that persisted in the defence of neoliberal political model) and of the left wing "neoliberalisation", a sector that, in the economic area, started to assume positions which, during the dictatorship, it had fought.

8.3. The Five Critical Domains of the Neoliberal Institutions of Governance

These are usually distinguished as five critical domains of institutional arrangements (CIDI, 2007) that are mutually related and interact during their evolution and adaptation:

1. The political domain refers to democratic rights, political power and participation that defines the citizenship relationships vis-à-vis the state.
2. The economic domain covers the access to markets and services, the organisation of livelihood strategies and the relationships among corporate actors.
3. The social domain refers to the formal and informal social networks and ties – based on trust, reciprocity and solidarity - that could provoke collective action.
4. The cultural domain particularly covers the identity constructions that shape the sense of belonging.
5. Finally, the ecological domain refers to responsibilities and responsible stewardship of the natural environment.

The different importance of these domains and their interlinkages are likely to be responsible for the specificity of prevailing institutional arrangements that shape the institutions of governance that have been built in Chile under the umbrella of the neoliberal model of development.

The analytical framework for studying institutional arrangement further concerns structural as well as actor-oriented aspects that reflect at least three analytical dimensions (Williamson, 2000; Granovetter, 1985):

i. Access to resources, information, power and networks: This first dimension provides insight into the opportunities or constraints for participation in development and its implications for chronic poverty and inequality.
ii. Rights, rules and responsibilities regarding governance regimes: This second dimension captures the internal organisation and external linkages that define a level playing field for institutional arrangements (usually as part of continuous struggles).
iii. Identity, culture and sense of belonging: This third dimension refers to aspects of (in)formal [formal and informal]??? embedment of the business neoliberal model that gives rise to:

    - Inclusion or exclusion (of firms and individuals) in the potential gains associated to trade openness and market liberalization,
    - The motivations for underwriting or fighting prevailing institutional arrangements, accepting or refusing their impact on citizenship at agency level.

These five-critical domains of institutional arrangements and three analytical dimensions to study them have been placed in the core perspective of this research and after some considerations about the role of exogenous and endogenous factors in the set-up of neoliberal institutions, will address hereunder.

8.4. The Political Domain: Democratic rights, political power and democratic participation

In order to analyse the specific characteristics of the political domain exhibited by the neoliberal model during the period under study, we will focus on four themes:

- The political construction of the neoliberal institutional environment during dictatorship period.
- The installation of neo-liberal political institutions in post-dictatorship Chile.
- The dynamics of adaptation and survival in democracy of the institutional environment of the dictatorship period.
- The mechanism of neoliberal capture of dictatorship government.

8.4.1. The Establishment of a Neoliberal Institutional Environment during Dictatorship Period.

As we analysed in previous chapters, the 1973 coup meant a strong institutional breakthrough for the Chilean economy and society with repercussions that were seen beyond the Chilean borders.

Authors like Perry Anderson (2003) assign to the Chilean military dictatorship the "merit" of having announced the unleashing of the neoliberal cycle worldwide in the present historical phase. Others like Harvey (2007), position the Chilean case as a world precedent, in which the experiment of the University of Chicago demonstrates the validity of its theories: "... served to provide a useful demonstration to support the subsequent turn towards neoliberalism both in Britain (under the Thatcher government) and in the United States (under the Reagan government) in the 1980s "(Harvey, 2007: 15). On the other hand, Chilean authors like Ffrench-Davis (2002) highlight the uniqueness of the Chilean process, noting that this is the main case of modern application of neo-liberal orthodoxy, given the purity, depth and extension of its coverage. Touting its long duration and the publicity made of its case worldwide *as success.*

The most attractive element of the Chilean model and to which its success is attributed, has been the creation of new rules of the game, that have shaped an institutional environment upon which (according to the champions of neoliberalism) its successes were built. However, as we have shown in the previous chapters, the implementation of these rules has not been able to produce the results that have been attributed to it.

Contrary to what had been promised, the institutional environment that has been created, instead of promoting mechanisms of resources allocation and distribution, endowed with a neutral and efficient character, operate as a tool of control of the Chilean economy for the benefit of the economic agents endowed with greater relative power.

Although the concentration of incomes and the presence of business groups controlling the Chilean economy are both a longstanding phenomenon, the new [in office] business groups have been materialized as such during dictatorship times.

During this period, almost without exception, these groups, came to reach a dominant position supporting themselves upon the neoliberal policies and on the easy capitalization

obtained from the privatisation (at low cost) of public assets and State-owned enterprises conducted after the coup of 1973 (Monckeberg, 2002; Salazar, 2015).

Nevertheless, some of the families and individuals that control those groups, had accumulated strong economic positions during the period of import-substitution. Its current power and insertion into the new model of development was a new phenomenon. In effect, the implementation of the neoliberal model of development, provoked the formation of business groups supported on the implementation of three **groups** of neoliberal rules of the game, acting as pillars of the new institutional environment

1. The first group of rules were supported under an umbrella macro-rule of the game which determined the domestic institutional environment as a whole; that is, the so-called "Subsidiary State Principle". Its adoption by the military dictatorship first led to massive privatisations of public enterprises; secondly, to private provision of public services originally delivered by the State; and thirdly, to privatisation of two environmental assets: The "non-produced assets" and the pool of "common goods".
2. The second group consisted of an articulated set of institutional arrangements, expressed as a system of market governance that ensured the dominance of big companies over:

    - Other types of companies (mostly MSME),
    - Workers, by limiting their capacities of self-organisation, and
    - Consumers, currently disorganised and devoid of any ability to face the power of market of large business groups.

3. The third group consisted in a hardly structured group of arrangements that transferred to private hands the totality of worker´s savings destined to finance retirements. The system of compulsory management of these funds by private organizations (named in Spanish AFP), allows the use of these retirement funds as cash flow for the Chilean business groups, who are the bond issuers of about 30% of bonds acquired by the AFP. This kind of arrangement, in a small market like Chile, placed the bulk of the country's process of saving and investment, in the hands of a particular economic group.

Based on the actions in each one of these large groups of arrangements, the Chilean business groups have consolidated, during the dictatorship period, a system of income extraction that has driven them to positions of world class economic power (Forbes, 2010).

8.4.2. The Gattopardo Times: The Update of the Old Regime´s Institutions during the Post-Dictatorship Period.

Even though the 1980 constitution is essentially an economic constitution, it has become the most important political tool that sustains the institutional environment set up by the dictatorship. The alteration of such rules of the context was an unachievable assignment without a modification of the 1980 constitution, a fact which situates the fight for maintenance or change of said institutional environment, fully in the political arena.

The total success of the Chilean transition process inaugurated in 1990 would have required from the new governments, to concentrate on the early and rapid elimination of the so-called "authoritarian enclaves" (Garretón, 1999) or "constitutional traps" (Atria 2013) left behind by the military regime. Evidently, this did not occur.

Those constitutional traps or deadlocks form a set of institutional arrangements inherited from the dictatorship and which, at this time (2017), have been only partially eliminated. However, this process of removal has taken more than twenty-seven years, alongside the extremely complex and unfinished process of expansion, centimetre by centimetre, of the democratic mechanisms within the new post dictatorship regime.[258]

258 The Pinochet control of the army, post 1990, is generally defined as the key variable that made possible consolidation of a neo-liberal political regime operating under a democratic-liberal facade. However, in our view at least, the maintenance of Pinochet's control over the armed forces (he remained as Commander- in- Chief of the army until March 10, 1998) was important, but only secondary part of the neoliberal political institutions after 1990. Many elements support the hypothesis that emphasises the role played by the presence of the former dictator as a key player in the new post dictatorship context. Firstly, this position enabled him to retain, through almost a half of the period that we analyse, large civilian and military support and other ardent enthusiasts of the neoliberal views that formed part of the social support of the dictatorship. Secondly, his status meant that neoliberal political forces had the material support of the armed forces, in a period when the high level of public political mobilisation may have attempted to modify the institutional framework. The ad-hoc mechanism, which designated Pinochet as commander-in-chief of the military, was not the only institution that lingered after 1990. Nevertheless, it was a transitional device useful to the neoliberal project only briefly (1990-1994). A Second minor neoliberal political institution was related to the difficulties of installing free election mechanisms at the municipal council level. Not until 1994 did, post-dictatorship governments reinstate the democratic election of municipal authorities. However, these elections did allow the direct election of council members, but only the indirect election of Mayors. Just ten years later in 2004, it was possible to choose Mayors in a direct way and in separate elections. However, there were others four substantial neoliberal-political-institutions, acting as the real deadlock to political change, and change on the economic rules of the game.

Those so called "enclaves" are mechanisms, which, contrary to other definitions, we denominate "political-neoliberal-institutions", were inherited from the old regime, and they correspond to an embodiment of the neoliberal vision of political representation within the organization of the Chilean State.

Our analytical perspective on that process essentially differs from Garretón's views (op. cit.). We believe that these gears are not strictly "enclaves" or "stains" on the "white robe of democracy". Actually, we are in presence of a sophisticated and comprehensive set of institutions of neoliberal governance which, far from being dismantled, after 1990 were consolidated.

For that reason, the so-called "enclaves", cannot be considered temporary authoritarian ghettos within an "incomplete democratic framework". On the contrary, they have been essential components of a regime "limitedly democratic", "only formally democratic", or "essentially not democratic", whatever definition you choose.

Nevertheless, the use of denomination of these deadlocks as "enclaves" is recurrent on the analysis of the Chilean case. Specialised literature (Garretón 1995; Fuentes, 2006; Muñoz, 2008; Campos, 2008; Siavelis, 2009) generally places its focus on the so-called "authoritarian enclaves", assuming that they constitute the last obstacle to the total democratisation of the country; a path which, slowly but unquestionably, has moved Chile to transition towards "full democracy".[259]

In our eyes, it is not enough to look at these enclaves in an isolated way considering them as a "dictatorship's residuals". Instead, we need to evaluate, side by side to analysis of the institutional environment, the bulk of rules and procedures (institutional arrangements) that act as boundaries to the evolution of an inclusive political and economic system, whose existence hardly can be attributed entirely to the dictatorship. In other words, we need to overcome the discussion about "enclaves" and address the issue of building of the governance of Chilean political system political system, its economic institutions and the country model of society built after 1990.

There is a direct relationship between the political system and the basic socio-economic conditions that make-up that regime. Democracy should not simply be conceived as a political regime, but as a form of organisation of power that affects several aspects of

259 Fuentes (2006) is one of the main authors that try to move away from this approach but is Hunneus (2014) who develop the more radical approach to this respect.

society. In the same vein, democracy should be visualised as a process of institutional strengthening grounded on an inclusive basis, a markedly different perspective from that of the neoliberals.[260]

The semi-sovereign and limited Chilean democracy only allow express the public will, if it is functional to the implementation of the neoliberal economics rules of the game that made essential part of it. Instead, if liberal democracy could make vulnerable the neoliberal's institutions of governance, it should be (in their opinion) hardly limited.[261]

The first so called "deadlock-institution" which post dictatorship governments inherited was the "binominal system". Not until 2015, was abolished the system who defined the positions of parliamentary representation. The "binominal" allowed which; the neoliberal right wing (or any electoral minority framed in a two-party system) was only required to obtain to 34% of the votes to achieve 50% parliamentary representation in each electoral district. However, when the votes of the unelected Senators (designated) are added, they may obtain 60% of representation with the 34% of the votes.[262]

At the same time, if one or more electoral districts, in which the centre-left wing had strong support, exceeded 67% of the votes, they could achieve 100% parliamentary representation in these areas. However, that hypothetical situation was compensated by the votes of the already quoted designated senators. Moreover, if that was not enough, it was offset by extraordinary quorum requirements (3/5 and 4/7) which had to be met in order to change the most important laws (Atria, 2014:61-62). These quorums were required by the 1980 Constitution in the event of the voting in of laws that could alter the economic model or change the Constitution. They made it impossible to legislate in such matters, a situation that allowed important distortion of citizen voting.

The new democratic governments faced complex tasks in order to advance towards the realisation of the political programme that had led them to a bloodless victory over the

260 In relation to that issue, we think that is necessary to stress the contribution of Chile´s new institutional arrangements to the maintenance of a neoliberal institutional environment, characterised by a distorted system of democratic political representation.

261 See footnote 20.

262 That was just the last of the distortions of the systems of political representation to be eliminated, because just in 2006 had ceased in functions not elected democratically senators (24% of the total), which strongly distorted parliamentary representation

dictatorship. The overcoming of the inequalities produced vis-à-vis the liberalisation process, as well as the inherited lack of participation of civil society in the solution of problems and decisions at different levels were presented as obstacles that often seemed insurmountable to civilian government's post-1990. Another serious issue was the lack of obedience to civil power exhibited by the police and armed forces, and their limited degree of support of the transition process. Finally, a last important issue that the new governments have had to face was the underhand resistance of the large business groups which controlled the Chilean economy. All these factors constituted a serious brake on attempts by these governments to translate their socio-political and electoral majority into an institutionally supported government with which they could effectively govern.

In general, the strategy of the new post-dictatorship governments has been extremely cautious and gradualist, favouring a tactic of specific negotiations in which every problem has been tackled singly, looking for parliamentary support but without developing a general strategy of confrontation with the set of authoritarian neoliberal-political-institutions. Without ignoring the significant political achievements that this strategy produced, at least for the first three post dictatorship governments, it implied an abandonment of its global goals, limiting them to calculations about short-term bargaining with the right- wing opposition, causing new governments to become highly vulnerable to the political distancing of social sectors than historically had been represented.

In recent years, some authors have argued that neoliberal-political-institutions during the transition exclude the development of a high-quality representative democracy, given the fact that Chilean political system is based on a Constitution devoid of real legitimacy. In the absence of a constitutional assembly, it has been argued that the Constitution does not represent people's preferences, only Pinochet´s willpower (Martinez and Ferrer, 2008). But some of these neoliberal-political-institutions are far from being attributable solely to the power and cunning of Pinochet.

On the contrary, new governments given the advantages that the neoliberal institutions represented for non-neoliberal political parties, do not confront these "enclaves", given that they damage the interests of their electorates but, at the same time, protect the stability of power positions of the new elite.

For that reason, the original conceptualisation of the "enclaves" works relative well when it refers to constitutional or institutional deadlocks inherited from the military regime and endorsed during the first post dictatorship period. Nevertheless, it is not so applicable when the concept is expanded to include the analysis of the democratic period as a whole, because it is inconsistent with the fact that, several essential neoliberal institutional arrangements were introduced between 1990-2009, thanks to the support of the centre-left MP, pressured in that direction by their own governments. (Fuentes,2012; Hunneus, 2014; Gárate, 2014;).

8.4.3. The Institutional Capture of Post-Dictatorship Governments

As we have seen in previous chapters, new democratic governments were soon trapped within a strange and unfavourable correlation of forces; the neoliberal-political-institutions prevented them from fully implementing their political programme, eroding their base of social support, and so making it increasingly difficult to achieve their goals using democratic means.

In fact, the new political elite that took power in 1990 endorsed most of the economic elements already in place. Thus, they validated the economic institutions created in previous years; nevertheless, eroding their political support. Moreover, in many cases those actions were defended, arguing that, the [uncertainty expectative] that existed within Chilean business groups (and former supporters of Pinochet's government) has not vanished, and therefore that could severely affect the process of investment and growth, a situation that they evaluate as dangerous for Chile's fragile democracy.

Since the beginning, new governments decided to focus their efforts on the gradual elimination of the authoritarian neoliberal-political-institutions, as a prerequisite to put in place a new institutional environment that lets them to implement structural reforms to the economy. However, in a few years, their tactical proposals turn out to be strategic and programmes of institutional transformation of the economy began to be perceived by them as "unrealistic and dysfunctional" to the growth dynamic of the Chilean economy.

Finally, toward the end of 2003, the attempts to reform the institutional environment had been abandoned and the policy promoted by the State had been reduced to promoting institutional arrangements, interesting but of marginal impact, which

although favoured the functioning of the party system and his style of administration of the state, which, however, did not aim at altering the non-democratic institutions that impeded the change of the neoliberal economic order.[263]

In sum, "La Concertación" preserved the core of the neoliberal institutional environment and perfected the institutional arrangements which the dictatorship had failed to tie and fully install before its conclusion. Their governments did not essentially modify any of the privatised structures of health assistance or pension funds, and they have not attempted any form of redistribution based on corrections of the uneven factorial distribution of income, the lack of market competition, the disadvantaged situation of MSME, the economic concentration phenomena, or the inefficient running of the educational system. They continue removing the State from the economic sphere as much as possible, excluding the discussion or the implementation of any kind of new development strategies or industrial policies, or of radical changes in the levels of competition with which the markets operate.

After analysing various historical cases in which there have been changes to the elites in power in countries with strongly extractive development models, applying and extending the so called "iron law of the oligarchies" (Michels,1911), Acemoglu and Robinson (2012:366) sustain. "*The overthrow of a regime presiding over extractive institutions heralds the arrival of a new set of masters to exploit the same set of pernicious extractive institutions. The logic of this type of vicious circle is also simple to understand in hindsight: extractive political institutions create few constraints on the exercise of power, so there are essentially no institutions to restrain the use and abuse of power by those overthrowing previous dictators an assuming control of the state*".

This assessment is applicable to the Chilean case in several aspects. However, the country´s internal situation is particularly intricate. Chile did not involve a scenario in which an old authoritarian regime was replaced by a new one that temporarily raised some democratic flags, but quickly ended up building a new dictatorship.[264] Nevertheless,

263 During 2003, three new and significant Chilean laws were passed. The first established a clearer career path and recruitment methods for public servant selection based on merit, aiming to reduce the scope of the government to appoint political allies to senior positions. The second provided public funding for political parties, and the third regulated private donations to political parties and candidates. These three laws were intended to increase transparency, reduce the scope for corruption, and allow the public sector to attract qualified people, but unfortunately, this was not the case.

264 The new post dictatorship Chilean governments has been so far to establish a populist-autocrat-

while the new elite lacked access to the core elements of economic or military power, the control of government and parliament gave them access to significant power to put in place neoliberal institutions able to produce (during 1990-1997) an impressive jump in the economic growth of Chilean economy, framed in extractive practices. Anyway, their success administrating the old neoliberal institutions began to offer to the new elite, politically based fresh opportunities that lets them to obtain further improvements to their political (and sometimes personal) arrangements, inaugurating in this way its capture by the neoliberal institutions of the Chilean model.

This path was propelled by corporate strategies developed by large private corporations, which supported on the neoliberal political environment in which they operated, had the freedom to dominate the process of the design and administration of institutional arrangements. In other words, during the period post-dictatorship period that we are analysing, the strategy of the Chilean economic group was oriented towards obtaining control of the new political authorities and the old political institutions in order to avoid changes to the institutions of governance of neoliberal model.

The foundations of this strategy are logical. The State is the main institution that creates or modifies the legal framework that defines, protects, or restricts firms' market strategies. (North, 1981; Weingast, 1995). That legal framework is not only the result of a purely economic cost-benefit calculation (Besley and Case, 2003). Some non-economic elements (historically-determined) also play important roles, such as the desirability of the regime in power, the rulers' strategies for political survival, the dominant processes of regime change, the country's social structure, international relations, the pre-existing economic regime, and internal power struggles (Przeworski and Limongi, 1993; Bueno de Mesquita, Smith et al, 2003; Acemoglu, 2005).

In the Chilean case, the complexity created by the intersection of several factors in a specific arena, closely watched by neoliberal institutions, made it easy for large firms to develop very efficient formal institutional arrangements and informal non-market strategies, to assure their growth or survival. In this way, the before analysed and so-called "political activity" of economic groups was quickly oriented to develop the kind of actions which authors like Hillman et al (2004: 838) define as "corporate attempts to shape government policy in ways favourable to the firms."

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authoritarian regime, in the style of Robert Mugabe in Zimbabwe, Daniel Ortega in Nicaragua or Chavez and Maduro in Venezuela.

The companies´ political activity in the economic field can take many forms. One is the appointment of individuals with connections to the government to their corporate boards (Hillman, 2005; Etzion and Davis, 2008; Davis and Coob, 2010). Another is the corruption of politicians and representatives (directly or through the financial support of political campaigns) in order to promote their own interests during the process of law-making. Research into this type of political strategy is still relatively unusual for countries outside the United States (Hillman, Nicholson et al, 2008; Lester, Hillman et al, 2008). However, recent studies have revealed the importance of the analysis of relationship between political activities and corporative governance in domestic and foreign firms operating in emerging economies, such as South Korea (Siegel, 2007), Brazil (Perkins, Morck et al 2008) and China (Li-Wen, 2012).

In the Chilean case, business groups have used the neoliberal-political-institutions inherited from the dictatorship to consolidate ideological and financial support in a specific political sector (the right wing). This ensures the maintenance of the neoliberal economic model, preventing the possibility of discussing the introduction of modifications to it. Moreover, the addition of some centre and left-wing leaders to their boards of directors; the financial support for their political campaigns; the ideological influence exerted by their well-funded think tank and the control over the media and the bulk of Chilean universities, have all defined their efficient agenda of co-optation of their "old enemies".

One core element of this economic strategy of co-optation is related to the influence that they exert on the overwhelming majority of professional economists of the country. This group, mostly trained at American universities, fiercely defends the neoliberal status quo; or disagrees with it only in accessory areas, creating a powerful intellectual force in defence of the neoliberal economic status quo. The control of these two elements has permitted large business groups to take control of defining "what issues must be discussed in Chile" and "what kind of new rules of the economic game", or "modifications of the old rules", can be adopted by post-dictatorship democratic governments. Nevertheless, the way in which large national business groups develop their non-market activities and the way in which large transnational companies who operate in the country utilise the neoliberal institutions of governance, are in several aspects very different.

8.5. The Economic Domain

All of the formerly described institutional arrangements (essentially of political order), has been the key that maintains the core of the neoliberal economic institutional environment and prevents any modification to said framework, which would encourage the deployment of barriers to the smooth operation of wealth distribution and resource allocation mechanisms put in place during the dictatorship.

8.5.1. Wealth Concentration and Institutional Freezing.

The levels of concentration of Chilean wealth in a few business groups, families and individuals are extremely high when we compare it to international levels. According to Forbes magazine's 2010 ranking, in Chile there are five families or people who own assets greater than 1 billion USD, and who are in the 100 richest people in the world. The combined wealth of these five persons/families (in a population of about 16 million) represents about 13% of the Chilean GDP. That is a higher level of wealth concentration than the United States, where there are only 406 persons/families with wealth exceeding the $1 billion (from a population of 300 million) within the ranking of 100 richest people of the world.

These elevated levels of wealth concentration are directly related to the big rules of the economic game established in Chile during the dictatorship and which are concentrated on the 1980 Constitution. However, these rules were refined during the Governments of La Concertación by means of the establishment of several institutional arrangements that we will analyse in this chapter, a process that has preserved the dominant position of large business groups in the Chilean society.

When the dictatorship ended in 1989, the new administrations emphasised their direct commitment to the Chilean people in order to establish the dictatorship and the neoliberal economists who would allow the economic concentration already described in former chapters. However, post-dictatorship governments were not completely persuaded to produce an institutional transition low quality institutions of neoliberal character to a context of a high-quality institutions detached from the strong factical powers that controlled the economic life. In fact, it ended up being easier, technically and politically, to simply take control of the extractive institutions, maintaining their essential features.

This dilemma strongly influenced the actions and notions of the new political elites, which were mostly captured by strategies of neoliberal economic elites. First, they forced them to adapt to the new system, then convinced them that the preservation of the neoliberal status-quo was good and, ultimately, allocated (legal and illegal) financial support to these new political elites (from de right wind and the centre-left wind). This process produced, within the new governments and its political parties, a decreasing interest in promoting process of substantial institutional change.[265]

8.5.2. Corporate Governance and Institutional Arrangements.

Several authors of different approaches estimate that in countries with relatively high level of government intervention in the economy, firms have to develop stronger political capabilities, because markets are not the key tool that defines which company prevails and which one fails (Granovetter, 1992; Ingram and Silverman, 2002:1-30; Mellahi., 2016).

Similarly, it is assumed that in countries where the government lets markets define winners and losers, companies are less focused on strategies highly driven towards political goals (Lenway and Murtha, 1994). However, Chilean experience does not fit with this vision in which the political role of companies is a direct consequence of a hostile action of the State towards market mechanisms.

Especially in countries like Chile, in which the dominance of market forces has reduced the role of the state to a minimum, and in which the maintenance of inherited rules of the game coming from the dictatorship times, tends to be enforced trough the blockage of democratising attempts that could potentially alter these rules. it is difficult to provide empirical evidence to support this point of view. In several countries that demonstrate these characteristics, the non-market activities of firms obey, in some ways, endogenous social, political and cultural factors at the firm level, which permeate economic life and are used as a strategy to achieve organisational goals that are more difficult or even impossible to fulfil in a competitive framework.

Chile is not, in this sense, exceptional. Political activity has become perhaps the most relevant non-market firm activity, widely used by large corporations that conduct activities in Chile, establishing the presence of high levels of corporate interventionism in the political arena.

265 From other side of political spectrum, the Chilean process numerous similarities with the stagnated Chinese process of transition to democracy, as it is analysed by Li-Wen Lin (2012).

8.5.3. The Multinational Business groups and their Corporate Institutional Strategies.

For a country like Chile, which receives large influxes of foreign direct investment from companies of diverse origins and features large national business groups that are more influential than the previous ones, it is important to elucidate whether the non-market strategies of Multinational Companies (MNC) differ significantly from the strategies of local business groups.[266]

Different investors represent countries with different institutional economic environments. This topic is of particular importance given that the most important and largest groups of MNC operating in Chile are: The larger MNC of Anglo-Saxon origin and the smaller Spanish MNC.[267]

Since the late-19th century, American and British investors have had a strong presence in Chile, particularly in the mining and manufacturing sector. On the other hand, Spanish MNC are relative newcomers, not only to Chile but also to the global economy in general.[268] Contrary to the British, American, or Canadian MNCs, the Spanish firms matured in a country dominated by business groups very close to the State. In general, these groups enjoy privileged arrangements that define the scale and requirements of public and private biddings used by public sector to buy its inputs (goods and services).

266 The foreign companies that established a presence in Chile during the years of openness and rapid economic growth, originate from various countries. Between 1974 and 2011, the largest investor in Chile was the United States, followed by Canada, Spain, the United Kingdom, and Australia.

267 The first group, includes companies such as the Australian Broken Hill; the British Rio Tinto and Anglo American; the American Electricity Company, AES Corporation; the Anglo-Dutch group Royal Dutch-Shell, the American, Americatel, owner of the national telecommunication company Entel; the American Exxon Mobil Corporation; the Swiss Nestlé; the British MNC London ED & F Man Sugar, controllers of Iansa (the only sugar-producing Chilean company), the British Unilever and others.

268 The Spanish MNC presence in the world only started after Spain's acceptance to the European Economic Community (EEC) in 1986 (Campa and Guillén, 1996). The entry of Spain to the EEC started a process of internationalisation of the major Spanish firms, leading to some becoming major MNC, such as Telefónica, Banco Santander, Entel, or BBVA (Guillén and Tschoegl, 2000; Salmon, 2001). The main geographic area in which these Spanish MNC invested was Latin America, with Chile receiving a significant portion of these investments (Guillén, 2004).

Similar to the events in Chile, Spanish business groups emerged during a long period of institutional re-arrangement led by a dictatorship (before Spain's entry to the EEC). Prior to their globalisation, the major Spanish firms developed strong ties with Franco´s dictatorship, frequently through the appointment of politically connected individuals onto their boards (Valdaliso, 2002).[269]

On the other hand, firms originating in the US, UK, Australia, and Canada, even though originating from radically different institutional contexts, developed their own political strategies (mostly through lobbying), but also established political connections by means of appointments of politicians as company directors.

The differences between both groups are not stark. The construction of networks of influence using politicians is not a strategy used only by Spanish companies. For instance, the Chilean Mining Council, the trade association of the large copper companies originating mainly from American, Canadian and Australian, has also used this strategy.[270] These two groups of countries may be typified by the kind of non-market practices that they use.

In summary, we can observe that for major foreign investors, the establishment of relations with the Chilean political elite has been developed through a mix of lobby activities and the appointments of directors. These directors ensure a fluid relationship with the sectorial authorities in charge of taking decisions that can affect their interests, regardless of the political nature of the current government.[271]

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269 From the beginning of operations until 2009, two former Ministers of Pinochet and the owner of one of the leading law firms of Chile, an attorney who played an important role as legal adviser to the dictatorship, were on the Board of BBVA in Chile. This practice is repeated in the main Spanish companies and since the restoration of democracy, has been extended to members of the new Governments and the leaders of their political parties. The most conspicuous cases were those of the Socialist leader Oscar Guillermo Garretón, who for almost a decade made part of "Telefónica Chile" directory; and since 2010, the former undersecretary of the Ministry "General Secretary of Presidency", Jorge Rossenblut, who is Chairman of the board of Directors of Endesa Chile, the privatised electricity company. This practice was so common in Spain and was used both during the dictatorship of Francisco Franco (1936–1975), and in the democratic regime that came after Franco's death, including the times when the left-wing Socialist Party ruled Spain (Cabrera and Del Rey, 2007; Pérez, 1997).

270 Of the six major countries that account for foreign direct investment (FDI), five are focused on mining. The only exception is Spain that does not invest in the mining sector.

271 Given the opacity of Chilean electoral finance laws there is little evidences of to the financing from MNC parties or candidates. However, the intervention of justice authorities has started to clarify

In general, the MNC have not been publicly associated with Chilean political disputes between post-dictatorship governments and their right-wing opponents. They exert their influence in the economic area alone, using the inhered rules of the game. They avoid making explicit any political position, as happened with the strong lobby of the mining companies, led by the Mining Council, during the legislative proceedings of the mining royalty law in 2005.

MNC influence has dispensed of any associations with the political efforts of the right wing in order to defend the neoliberal political institutions (or the neoliberal model of development). Foreign investors have been passive users of the advantages given them by the inherited economic institutions, looking to enhance economy-specific aims, e.g. their efforts to maintain laws that allow foreign and private participation in the large-scale copper´s mining, or maintain the generous tax and regulatory framework that favours them.

In other sectors, the most important area of foreign investment (of USA origin), beyond mining interests, is the retail sector. In this area, Wal-Mart Corporation has invested at least US$4.5 billion in the acquisition of 99.72% of D&S holding. The interests of this North American enterprise have been strongly differentiated from the political approach of their former owners, the Ibañez group, headed by a traditional Chilean family with strong political weight in the right wing. Wal-Mart has concentrated their lobby efforts only in defence of economic norms that favour their interests, in a manner very different from the political approach of the right-wing Chilean businesspersons.

Spanish investment, on the other hand, has been sectorial, concentrated in the field of provision of public services (water, electricity and telephony) and in the banking sector, showing great audacity in establishing political ties with leaders from all sectors, directing them to the protection of their corporate interests, at that time supported by the inherited economic institutions.

In general, Spanish MNCs do not attempt to influence politic activities in a direct way, nor publicly defend the authoritarian neoliberal-political-institutions. However, these Spanish companies are notorious for recruiting the bulk of their senior Chilean officers from the Pinochet supporter's elite.

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the presence of this kind of MNC political involvement. See: http://www.latercera.com/noticia/nacional/2015/05/680-631460-9-aguas-andinas-pago--341-millones-a-entidades-ligadas-a-la-alianza-y-nueva.shtml

In sum, we can say that MNC of Anglo orientation are focused in work in Chilean market using the inherited institutional arrangements and develop a heavy level of lobbying activities in order to freezing up any institutional change that may affect their profits. On the other hand, Spanish and others Continental European MNC have followed another path. They are not particularly focused in defend the already existing arrangements. In fact, they prefer establishing close links with the political and economic authorities in order to catch a market share on business areas depending of the State (utilities, infrastructure, military weapons and regular government purchases). In general, the arrangements in which they are interested are mainly those that affect government's purchases or private business operational cost, but their business model hardly may be defined as predatory, except in the environmental area.

There are few MNC operating in Chile who meet at least four of the six characteristics that we have selected to define how predatory business model is, instead of national origin groups is quite frequent to observe not only four, but even the seven characteristics within their business model.

8.5.3. The Chilean Business groups and their Corporate Institutional Strategies.

If we investigate Chile´s wealth distribution, at the end of analysed period (in the year 2009), a set of 33 business groups, mostly of Chilean origin, controlled the Chilean economy.[272] Ten of these were very important in terms of their market power. The other twenty-two, regardless of their relative influence, possessed much less economic weight than the first five groups, expressed in Table 8.1, who comprise 50% of total asset value.

272 Despite its influence on the Chilean economy, the TNC (trans-national corporations), mining and non-mining, are not considered as business groups here. There are two reasons for this. Firstly, they do not list their shares on the Chilean stock market. For this reason, from the national perspective, they exhibit unified property. Secondly, they constitute unique companies that are not part of a network of related companies, operating under the control of a group of shareholders, whether majority or minority.

Table 8.1. Ranking of Chilean Business groups

RANKING First Trimester 2010	BUSINESS Holding NAME	CONSOLIDATED ASSETS VALUE in MM US$ First Trim. 2010	BUSINESS HOLDING STRUCTURE
1	LUKSIC	56.647	Family Holding
2	MATTE	38.824	Family Holding
3	YARUR	31.099	Family Holding
4	ANGELINI	29.920	Family Holding
5	SAIEH	23.658	Family Holding
6	SAID	20.659	Family Holding
7	SOLARI-CUNEO	14.081	Family Holding
8	PAULMANN	13.559	Family Holding
9	SECURITY	10.866	P.L.C. Non Family-Controlled
10	HURTADO VICUÑA,	9.830	Family Holding
11	CGE	8.119	P.L.C. Non Family-Controlled
12	CUETO	7.110	Family Holding
13	PONCE LEROU	5.943	P.L.C. Non Family-Controlled
14	FERNANDEZ LEÓN	4.889	Family Holding
15	NAVARRO	4.601	P.L.C. Family Holding
16	PENTA	4.518	P.L.C. Non Family-Controlled
17	CAP	3.961	P.L.C. Non Family-Controlled
18	CALDERÓN	3.410	Family Holding
19	LARRAIN-VIAL	2.857	P.L.C. Non Family-Controlled
20	SIGDO KOPPERS	2.171	P.L.C. Non Family-Controlled
21	CLARO	1.686	Family Holding
22	BRIONES	1.675	Family Holding
23	GUILISASTY-LARRAÍN	1.585	Family Holding
24	SALFACORP	1.526	Multi-Family Holding
25	BOFILL-CAROZZI	1.363	Multi-Family Holding
26	GRAS-SOCOVESA	1.243	Multi-Family Holding
27	EMBONOR	851	Multi-Family Holding
28	BEZANILLA	768	Family Holding
29	NAVIERAS	761	Multi-Family Holding
30	SWETT - FORUS	724	Family Holding
31	MULTIEXPORT FOODS	450	P.L.C. Non Family-Controlled
32	TATTERSALL	377	P.L.C. Non Family-Controlled
33	LECAROS MENENDEZ	373	Family Holding

Source: Author´s elaboration based on FECUS of Superintendence of Stocks and Insurances.

In developed countries, largely those who belong to the OECD, the property of enterprises and the business groups are extremely atomised. The main problems linked to their corporate governance are the typical problems of agency, in which there is conflict of interests between those persons who play the work of management, and shareholders, mainly the minority, who are more exposed to these problems.

In Chile, the situation is very different, 33 business groups generate around 60% of the GDP. Within those holdings, only nine have majority shareholders who are not integrated in a structure of family business (in dark colour at Table 8.1.). The remaining 24 business groups build up 87% of the asset value and all have family structures.

This last set of business groups are directly controlled by families who have major share packages traded on stock exchange, a fact that gives to these families the control of these business groups. Within the group, we can also find others corresponding to multi-family structures, in which one family assumes a leading role with regard to the remaining partner families.

This highly unstable structure has resulted in a wide configuration of alliances between family groups, according to successive transfers, sales and mergers of companies, which are usually nucleated around any financial institution.

On the whole, the Chilean business groups are familiar in nature, but members of these families are not related to the ownership of their companies as individuals, if not through other companies or holdings, which are not always 100% owned by the same family´s group. There are groups in which there is no one family connected directly, but rather several families or even people not related by family ties. This situation occurs in the following business groups: Security, Penta, Ponce Lerou, CAP, CGE, Sigdo Koppers, Forus, Multiexport Foods and Tattersall. All the other groups are closely controlled by family or multi-family structures, with minimal external participation.

Half a century ago, in a pioneering work, Lagos (1962) warned that the configuration of the Chilean capital was concentrated in the large estates, banks and industry. Two decades later, the Chilean economy showed important changes in property, but not in the patterns of capital accumulation. The nationalisation of banks and large firms during the Allende government, the subsequent return during the military regime and the first wave of privatisation dictatorship (1974-1978) and policies of trade openness

promoted by neoliberalism, affected the composition of the old business groups and their property structures.

The neoliberal policies particularly weakened the old industrial economic elite. The new market governance modalities favoured large business groups operating in the financial sector, because they obtained access to international financial markets at low rates, and could borrow from local businesses at conveniently high rates (Arriagada, 2004).

After that, the financial crisis of 1982 produced a new and dramatic turnaround. Several traditional groups, mostly in the textile sector, lost their enterprises because of this crisis (Yarur, Hochschild, Sumar, Hirmas and Pollak). Other groups who had greater financial access, (Angelini, Matte, Said and Luksic) began a process of the take-over of companies in bankruptcy (Lefort, 2010) or the substitution of the old national production of the bankrupt enterprises, managing a process of substitution of national production by imported goods. Three or four years later, a second wave of privatisations arrived (1985-1988) and many public companies created by CORFO, like telecommunications, energy and air transport, began to be privatised.

Participation in privatisation required enormous purchasing power. However, because of the financial crisis of 1982, the Chilean private sector did not have access to these kinds of resources. The partnership with international capital, and the authorisation of private pension funds (AFP) to buy shares in privatised companies, allowed some national conglomerates to expand their areas of influence. Indeed, the private firm administrators of pension funds (AFPs) became one of the largest shareholders of companies privatised since 1986 (Gárate, 2012).

In sum, the implementation of the neoliberal model by the dictatorship favoured the emergence of new business conglomerates that introduced important changes to the domestic landscape of the economic class, changing the role of large enterprises as social actors by means of the introduction of different features to the Chilean corporate culture. One of these features was the consolidation of a neoliberal ideological and economic vision that become predominant amongst the corporate elites, as well as in their relations with the technocratic or academic groups related to them.

However, in our view, emergence and enforcement of Chilean business groups was not a situation produced by the application of the set of theoretical positions grouped

behind a neoliberal agenda of development. The evidence provided until now shows that behind of this set of ideas are the interests of some powerful social groups centred on securing the market power of a small group of large companies. These large firms, which nowadays control the bulk of Chilean GDP and which, after the 1973 coup, also took control of the bulk of the State-owned enterprises and of the whole of the natural resources that were privatised. In fact, they took control the main sources of Chilean political and economic power.

The neoliberal program has become a rationalisation of the social and economic interests of these business groups. Therefore, it is not correct to assume that we are in the presence of a simple set of polemical ideas, which incidentally led to benefit a particular social and economic segment. The Chilean neoliberal program is more than a mere economic program, is an institutional program which, since 1973, has constructed new rules of the economic game and institutions of governance that strengthen these rules, and a political institution that has been very efficient in preventing any possibility of dismantling such institutional structures at the end of the dictatorship. The strength of the set of economic institutions installed in Chile, reflects the control of the different powers of the State by a handful of large companies, which have achieved solid positions of economic and political power during the application of the said model.

These companies are organisations but, taken as a whole, they are concentrations of market power, which may give rise to concentrations of wealth. It is not surprising, then, that the large Chilean companies became organisations which encouraged institutional structures of power functional to the interest of their owners, in a very similar way to the situation described by authors in comparable contexts (Crouch 2008:70). This is a situation, which, in the Chilean context, has assumed the form of extractive institutions, which inhibit development, rather than creating market structures to promote it successfully.

A significant point relates to the mechanisms of distinction and reproduction of the economic elites. Within these groups, an essential condition in developing successful economic activities is their subscription to a framework of the social, family and religious relationships existing in this segment. An important role in that sense has been played by fundamentalist catholic orders, like "Opus Dei" and "Christ´s Legionaries".

That option implies the absorption of certain life styles that were highly different to those of other Latin-American elites, who are more liberal and open minded and less interested in ideological issues. One of the most important features linked to these stipulations, which is present in many studies that analyse is, is the merger existing in that sector between the traditionalist catholic conservatism and neoliberal thought (Catalán 1979; Fisher, 2009; Cristi, 2015). This merge allowed them to culturally resist, in a partisan way, the liberalisation process that follow the end of the dictatorship.

From another perspective, some studies have focused their attention on the analysis of the political and social participation of the economic elite (Montero, 1997, Arriagada 2004; Hunneus 2001; UNDP 2004; Belt 2004; Gárate 2012), or in the economic practice associated with to the origin of the different business groups.

In general, we consider the proposal of Montero (op. cit.) is perhaps the most useful approach to the structure of the business groups in the 90s. She classifies some groups as traditional conglomerates and others as emerging groups. Traditional ones are supported in pre-existent productive activities, which arose because of the privatisation of public enterprises. On the contrary, emerging groups are financial-services focused. They took control of new activities in the banking sector during the 1980s, including: the insurance sector, the privatised educational institutions, the administration of retirement funds, or in private provision of health services.

Within the first group (traditional), Montero identifies family groups that became holdings that are grouped around some family leaders that assume the holding control directly. That is the case of Matte, Paulmann and Sahie groups. In other groups, the family chief is only partially involved in the management of their enterprises, operating mostly indirectly through professional managers, as it happens with Luksic, Angelini and Solary business groups.

In the second group (emerging), Montero includes new economic conglomerates who build their holding by leveraging their control of certain financial institutions. These new groups emerged with the development of the capital market, beginning with financial companies, passing then to the ownership of privatised banks in 1975-76, and from there to ownership of privatised companies. Overall, financial openness to the global financial markets allowed that these emerging groups, whose power rests with a few executives, with a specific expertise and who were officials of

the dictatorship, to take charge of the utilities public enterprises and some financial entities that were privatised.

Many business groups in this last segment (emerging), consolidate their positions as a direct result of discretionary decisions by the dictatorship, and they have been benefited from the process of privatisation by means of the appointment of members of this group to public positions of power. From there, they frequently defined rules and norms which enriched them and consolidated them as business groups.[273]

For the traditional groups, it has been sufficient to use defined general rules that benefit them indirectly, by creating an environment that could not have existed without the support provided to them by neoliberal economic institutions.[274] The emerging business group needed ad hoc institutional arrangements in order to consolidate their positions and most of their high-level staff have played a critical role defining those arrangements from top positions within the dictatorship bureaucracy.

Another essential difference between the two business groups (conservative and progressive) is the different proportion existent within both of them, between export-oriented firms and domestic market oriented firms. Both kinds of firms have benefited *directly and indirectly* from the rules of the game created by the dictatorship. But, for domestic market-oriented oligopolies, the neoliberal rules of the economic game have constituted an essential element of their success.

Regardless, the neoliberal adherence of both groups is indisputable. They support political campaigns and right-wing think tanks. In general, the institutional focus of traditional groups is more oriented to the defence of economic neoliberal-political-institutions, but the emerging groups are additionally active giving support to political neoliberal activities, because they are not only committed to give support to the economic model proposed by the neoliberal approach. They are strongly linked to neoliberal values and its ideology as a whole. Overall, we can observe that there are few large business groups who have not ventured into external markets, even those whose

273 Molina (2005) shows that five of Chile's largest business groups would be owners, directly or indirectly, from the 47.6% asset value of the companies listed on the Santiago Stock Market.

274 For them, special mention should be made of the capital biased labour laws, the norms that regulate the relationship of larger enterprises with their MSMEs providers, and the weak consumer protection laws.

core economic interests remain in Chile, in the comfortable position of oligopolies in domestic markets.

This double position, for both kinds of business groups, has made it possible for them to capture markets and trade channels that once belonged to the MSME, and at the same time, expand their market influences off-shore.

The market power of main business groups is mainly founded on the takeover of MSME's market share, and of the share of large enterprises of minor size. Their position allows them to drain defiant firms of their working capital, upholding them as captive customers of banking, charging higher interest rates and being over-demanding in terms of guarantees.

Those elements, in both segments, have played a central role in the building of their position of economic dominance. Independent firms (MSME and larger ones) that have been incorporated into the interior of the value chains of retail larger companies (exporters and non-exporters) tend to be subject to predatory trade relationships. Thus, the decline of this segment of small enterprises and the strengthening of larger retail groups, growing at their expense, are part of a unique phenomenon.

Altogether, we can conclude that both kinds of business groups, despite their different political profiles, share a common role in the economic area. They act as gatekeepers to market access, controllers of network governance and as a restraint on the upgrades necessary to facilitate the integration and coordination which these export activities require if they want to be successful beyond the national boundaries.[275]

275 The two key elements to moving up in the global value chain perspective are the acquisition of capabilities and access, not just to markets in general, but also to particular marketing channels. There is a certain minimum level of capability required before a firm's access to global markets can be achieved. The new entrants can take advantage of learning effects within global value chains, arising from supplier-buyer interactions. However, the action of the big exporting groups has severely limited this potential to the point that by 2015, less than 1% of the value of exports came from MSME, avoiding their entry into global value chains which could exert a positive impact on technological capability and upgrading, and promoting learning by new exporting firms.

8.5.4. The unequal LSE-MSME Arrangements as a Source of Capital Accumulation.

The dynamic of MSME´s spoliation rests on the presence of a set of three kinds of institutional arrangements, in appearance of importance:

i. The rules that define the competitiveness of market credit and capital markets, which allow the concentration of the credit in large companies and a sort of credit rationing to the MSME, which also face interest rates overvalued, due to lack of interbank competition.
ii. The absence of anti-trust rules, in the style of the USA Robinson-Patman acts, which limited the practice of price discrimination based on volume of purchases. This is a procedure commonly used in Chile and that disadvantages the MSME who, as a result of the higher cost of their intermediate inputs, are subject to production costs higher than those of their larger competitors.
iii. A regressive tax system that allows smaller companies to pay proportionately more corporate taxes than large firms that concentrate the largest percentage of sales and profits (SII, 2009).[276]

From these three large groups of arrangements it is possible to differentiate at least six kinds of arrangements which act institutions of governance of each one of the areas in which they are running.

8.5.4.1. The Financial and Credit Arrangements.

Other institutional arrangements are those that favour the lack of market´s competition given the presence of the extreme concentration of credit which acts as rationing driver. There are multiple causes which constrain the credit available to MSME; the main ones being of institutional character. If we focus our attention on the institutional factor, we must emphasise at least four of them:

276 In Chile, between 1990 and 2009, the tax paid by all companies ("First category tax"), was on average 12.2% of the total taxes collected by the State. The remaining percentage corresponded to: VAT-Tax (on average raised 49%) mostly paid by low-income persons; Banking Loans-Tax (which on average raised 13%), Alcohol and Tobacco Taxes (on average 12%) and the Import Tariffs (which on average raised 7.2%) even though from 2009 onwards this tax tended to raise 0% to eliminate the tariffs, product of the FTA). Nevertheless, large companies paid 65% of first category collected taxes, whilst 35% was paid by MSME. Given that LSE produce about 85% of the profits and the MSME less than 15%, this tax distribution is highly regressive.

- The risk classification system of banking loans defined by the Superintendence of Banks, which requires financial institutions to set high levels of reserves associated with loans to MSME, making it more expensive to give credit to this sector.
- Government reluctance (supported by the Banks) to establish a national system of "mobile guarantees", which would enable companies to move their credit to banks that offer better credit conditions, thus encouraging interbank competition.
- The presence of a monopoly on electronic payment system which obliges them to pay high percentages of each transaction to the Banks by way of operation fees which, constitute a kind of "private-sales-tax.
- The high interest rates charged for consumer loans and credit cards administered by banks, tend to be additionally raised when retail chains focus on the segment of people not subject to credit by banks,[277] whom receive direct credit from retail stores that utilise higher interest rates than the banks.

Those arrangements are associated with an additional one, resulting from presence of an oligopolistic media market. Its advertising encourages growing expectations of consumption in the population, which are satisfied by credits and loans that are not always sustainable.[278]

The institutional arrangements that permit the oligopolistic performance of media markets are based on the absence of a "Media-Law" which could exert a regulatory power. That legislative initiative is trapped at parliament and, for that reason, concentration of media property and advertisement spending (public and private) in still concentrated in a few media enterprises, without any restriction.

8.5.4.2. The Privatisation Arrangements.

Between 1973 and 1989, 15,888 real estate properties belonging to the state were transferred to private hands, of which 11,000 were transferred directly, without any

277 The term used worldwide is "Ninja customers": People with no Incomes, no Jobs and no Assets.

278 We should recall that the average s monthly salary of a Chilean worker (in US$, 2016) is around US $500, by which high interest rates amount to a large share of their incomes during many years of work, in order to meet the needs of short-term consumption. This phenomenon additionally discourages the incorporation of worker's unions, because it could jeopardise the individual capability to obtain long-term incomes that would allow them to pay their debts.

payment. 80% of the expropriated lands allocated to farmers during the land reform were also transferred to private owners, of whom only 28% were former proprietors (Silva, 1987). In the urban sector, 725 large State-owned enterprises were sold at low market prices; the sum of the financial loss of the Chilean State from all public goods transferred, as determined a Senate Standing Committee (1990), amounted to 6,000 million US$ as of 1990.

During the analysed post-dictatorship period, the on-going privatisation process increased. The area most affected was the most important for the Chilean economy: copper mining. Towards the end of 1990, Codelco (the state mining company) produced about 90% of the copper in Chile. However, at by the end of the year 2009, they only produced 30% of the Chile's copper. The remaining production was by private companies, mostly transnational, who were granted mining concessions by the Chilean State.

In the post-dictatorial period, two sub-periods can be distinguished: The President Aylwin (1990-93), and the following administrations (1994-2009). During the first, the stock packages of only six companies were sold which ended, most significantly, the transfer of ownership of electricity companies that remained in the hands of the State. e.g. Endesa, Peuenche and telecommunication companies like Telecom, CTC and Entel.

The second period presents a somewhat different picture. Between 1994 and 1998, the process of privatisation of the national air company, LAN Chile was completed. The National Radio, the railway company Ferronor, the electricity company, Edelaysen, the public company of marine cabotage (Empremar) and Minsal (a public lithium mining company), were also fully privatised. All these processes were followed by a reduction in the participation of the public sector in the power generation sector: Colbún Machicura and at Tocopilla S.A. (suppliers of electricity to Codelco), the port of Lota, and the sanitary services companies of the southern cities Valdivia (Essal) and Concepción (Essbio) were also all sold. In addition, foreign capital was incorporated to Edelnor (Southern Electric-USA) and Colbún-Machicura (Tractebel-Belgium), in a process of growing privatisation of the public firms of electrical generation,

Drinking Water companies were already considered for privatisation in 1989: 11 regional corporations had been created to facilitate the privatisation. Emos and Esval, the biggest ones, had been privatised in 1988 when the regulatory framework

(DFL 382 and DFL 70, promulgated in May 1990) had been approved. However, the Government of President Aylwin, who proposed a new regulatory framework and some amendments to the relevant legislation, blocked its transfer to the private sector.

MNC were waiting until 1997; after this year, privatisation began. In higher education, although there has been no "privatisation", in the sense of the transfer of assets, the sector began to rapidly privatise the educational supply by means of:

i. An increase in the relative weight of private universities, and
ii. A decrease in the relative weight of the public financial transfers within the total revenue of the public universities.

The same has happened with the private provision of health services and with diverse other services formerly provided directly by the state.

8.6. The Social Domain.

In this domain, the relationships between agents are mediated or conditioned by "social norms", "laws", "rules", "customs", "contracts", "collective agreements", "organisations", etc.: in short, by what we have called labour market governance institutions.

The governance institutions play both a positive and a negative role: they may limit or correct the appropriation of rents (which is related to the correction of market failures we talked about earlier); and they also may allow or foster that same appropriation.

In our analysis of the Chilean case, we have seen that the labour market's social institutions create rents and, at the same time, the possibility of opportunistic appropriation of those rents. This is what makes the labour market's "social" dimension so controversial. In general, the neoliberal thought asses that correcting an inefficiency may create other inefficiencies, even injustices, and introducing solidarity may be inefficient and end up causing opportunistic and self-interested behaviours. In same aspects that view made a strong point and for that reason is needed to understand the dynamics of the processes whereby Chilean institutions were created and are evolving.

Of all the different aspects of these processes, we have concentrated on individual and social learning. Conventional economics explains how equilibria are achieved in the

short and long term, ceteris paribus the institutions and assuming that social values and norms are irrelevant or, alternatively, that they do not change. However, these equilibria do not consider the learning we mentioned earlier, at least not much of it, not the most important part.

We can conclude, therefore, that the discussion about neoliberal model, should take this learning into account. And we have pointed out that at least part of this learning is embodied in higher-order institutions, including social norms, some of which – those that have an ethical content – seem to have the mission of establishing the conditions for a long-term meta-economic equilibrium, because they are institutions that correct "institutional failures".

8.6.1. Control of the Pension Funds and Saving –Investment Cycle.

Starting from May 1981 inspiring on neoliberal principles applied to the fields of pension savings and social security and health insurances, Chile inaugurate a system of retirement funds based on individual capitalization mechanisms, with a compulsory contribution for the workers dependent on quality of new affiliate. Social security contributions must be paid only by workers, with the exception of the costs relating to the social insurance of occupational accidents and occupational diseases, which are still in charge of the employer contribution; rate was established in 10% of taxable remuneration. These liquid resources are allocated to the individual capitalization account, more a quote that covers insurance for disability and survival and a Commission to AFP.

The AFP used one smaller part of the cash collected each month to pay pensions to those who are already retired. Another part is invested in bonds of the State and the bulk of the money raised is oriented to loans to LSE. At December 31 of, 2009, the fund´s resources managed by the AFP amounted to 118 thousand million dollars of which, 66.4 thousand million dollars were invested in Chile and 51.6 thousand million dollars overseas. These amounts are extremely high for the size of Chilean economy, constituting a source of cheap and accessible financial resources to the large business groups which, using the previously established arrangements, do not absorb it in its entirety, only since it lacks capacity to absorb more investments in a market as small as the Chilean domestic markets are.

8.6.2. The Labour Market arrangements.

The consolidation of a labour's value-added extraction system is allowed in Chile on an institutional basis centred in specific arrangements:

i. A Labour movement lacking the legal possibility of organising union power.
ii. The validity of the extant labour-laws of the dictatorship and of the accrual of minor new formal rules that prevent unionisation and collective bargaining.
iii. The possibility of enterprises to hire substitute personnel when the firm is subject to strikes.
iv. The option of dividing a single company into tens or hundreds of paper companies, associated with different tax codes, avoiding giving muscle to trade unions.[279]
v. The use of the MSME as element of decompression of wage pressures and a provider of labour of lower relative price

These are examples of the main institutional labour market arrangements oriented to disincentives workers' organisation, inducing them to be reluctant to join a union and so maintaining the downturn of labour remunerations in the large-scale sector.

8.7. The Cultural Domain

Social institutions are a system of behavioural and relational patterns that are densely interwoven and enduring, and function across an entire society. They order and structure the behaviour of individuals by means of their normative character. The ability of these groups to install their ideas in the main areas of the cultural, social and economic fabric which, in the past operated independently of their interests (e.g. education, health, government), has strengthened its position of power. Ownership of the media, universities and their close links with the hierarchy of the Catholic Church, has also strengthened the symbolic power of these elites.

That is why it is not surprising that, with the return to democracy, neoliberalism remained hegemonic, and even deepened, although economically it only achieved

279 In Chile, each formal enterprise has a unique tax number, denominated RUT (in Spanish, Rol Único Tributario). It is only possible to build trade unions in each RUT-enterprise, but if one large enterprise is artificially divided in several RUTs, the trade union became impossible, or at least lack significant force.

an average annual growth of 2.9% of GDP in 16 years, with falls of the order of 17% and 14% of the GDP in 1974 and 1982, reaching the historical peaks that have record in unemployment in 1982 and of economic inequality in 1987 (Ffrench-Davis, 2014). Only an ideology fully rooted in our consciousness could survive that.

8.7.1. The Political Making of a Neoliberal Cultural institutions.

The Chilean situation, in the analysed years, constitutes a good example of how actors and institutions are constituent and mutually interdependent entities which define features of the institutional environment. We may assume, as Searle (2005) and Hodgson (2006) define them, that institutions are structurally similar to an iceberg, in which the part above the surface is composed of formal rules, boundaries and procedures, whilst beneath the surface rests a mass of social conventions, symbols, rituals and meanings, from which the actors interpret the world that surrounds them. This aspect of informal institutions plays a central role, given the fact that the formal rules of the game can end up being accepted unquestioningly (Meyer and Scott, 1992). The institutional environment is a mix of both kinds of institutions.

Following this shared approach, we believe that individuals are socialised into a certain perspective of the world, not merely by formal rules, they learn many social conventions informally and, from them, they build an accepted way of doing things. This process, by which informal rules contribute to uniform behaviour and facilitate social interaction, is essential to the process of institution building. Thus, formal rules and informal institutional traditions are constituent parts of the process of constructing the "imaginary institution of society" (Castoriadis, 2007). This means that both kinds of rules are mutually interdependent elements, which constitute the frame of reference, or institutional environment, within which individuals explain the world that surrounds them, and which enables them to be a part of an objective reality (Meyer and Rowan1977; DiMaggio and Powell, 1983).Therefore, these rules of cultural action or values, associated with formal and informal levels of conditioning, acquire rationality through the processes of interaction between different actors, until they reach a level of consolidation, or institutionalisation. This determines the configuration of their perceptions and interests and the type of relationships that occur between them (Fleetwood, 2008).

As a result, the perception of the world that individuals have is largely determined by the institutions in which they operate. If any procedure or course of action does not

exist or is evaluated as "unrealistic", that makes it non-existent when viewed from the perspective of some individuals, and it becomes impossible for players to consider it as an alternative. As a result, individuals and even organisations, like political parties which, as all organisations are institutions after all (Linarelli, 2010), can only act in the world based on the values and the knowledge which provides them with the specific institutional framework within which they are immersed, defining their particular views on reality. The political sphere is the main space in which formal and informal institutions interact, and politics is greatly influenced by the national specificity in which this activity is immersed according to the previous definition. This sphere constitutes the principal arena in which formal and informal institutions interact to influence economic and cultural life as a whole. This double iteration of both kinds of institutions assembling the big rules of the game is clearly illustrated by the history of the Chilean transition to democracy.

Over the 17 years of the dictatorship in Chile, despite the enormous power of its dictator, the uniqueness of the Chilean regime compared with other Latin American states consisted in its strong institutional seal. The axis of the policies of that period was not structured around the consolidation of the personal power of Pinochet, but around rules of the game that transcended his personal interests, but not the interests of the business groups that formed his base of support, to which, ultimately, the dictator and his technocracy answered.

8.7.2. The Running of Cultural institutions of Neoliberal Model

This neoliberal logic is extremely detrimental to citizenship in both micro and macro levels. In this regard, at the micro level, it is possible to verify it in the education system, where a significant percentage of the population receives an education with deficient academic performance, on the one hand, the abandonment of the State with its public facilities for reasons of minimization, and on the other hand, from subsidized private establishments that, by operating with business logic, minimize costs that are required to improve the quality of education. Meanwhile, a very minority proportion (totalling 7% of enrolment), accesses an education with good academic performance and can pay for it.

In health the same thing happens, where it was also institutionally designed that those who could pay for health could be treated in clinics, and who could not, then they should be treated in public hospitals. The differences between the two attentions

are as significant as the difference between the performance of private educational establishments paid and public lycées.

In the pension system, the individualist logic also turns out to be detrimental to that majority percentage of the population that, for socioeconomic reasons, has not been able to quote uniformly for 30 years, nor to accumulate large sums of savings, since they receive remunerations that border the median of Chile, which fluctuates around $340 thousand pesos.

In the macro, the neoliberal logic also turns out to be detrimental to our model of economic development. The State minimization, in addition to pauperizing its services in education and health, has lacked a strategy to economically develop the country. This challenge has been left in the hands of private companies that only look after their own benefits, functioning in a disjointed manner and without a common purpose. Evidence of this is that we continue to have a strategy of exporting mostly natural resources of low added value. We have had this strategy for a large part of our economic history, and have recorded painful economic failures for our people.

It is worth remembering the international crisis of 1875, which brought down the prices of our star raw materials, copper, wheat and silver, by about 50%, nearly caused an economic collapse that was only avoided by the income from nitrate territory to our country, a resource that became our new star export product. However, again in 1929 there was an international crisis of proportions that made our economy the worst hit in the world according to the World Economic Survey, with falls in GDP that took 20 years to recover.

Today we continue with the same strategy. Nearly 50% of our exports depend on copper, similar to the 68% that nitrate [pondered] in our exports of 1920 (McQueen, 1924). The rest is mostly natural resources with low added value. The danger of this low productive diversification is the enormous vulnerability to which it exposes us. A crisis like these could happen again, as the crises of 1998 and 2008 reminded us.

Since the private sector is comfortable with this model, the State must play an important role in the diversification of our productive matrix. Assuming both promotion and productive roles, it must promote strategic industries that promote economic dynamism. There are many myths that this strategy was a failure in our history, since after the crisis of 29 a different development strategy was opted for: industrialization directed

by the State. However, between 1950 and 1970 the annual growth of GDP reached 4%, higher than what was recorded by the neoliberal period during the dictatorship, and equivalent to that registered in the last twenty years of reformed neoliberalism.

That is why it is not surprising that, with the return to democracy, neoliberalism remained hegemonic and even deepened its institutional hold, although economically it only achieved an average annual growth of 2.9% of GDP in 16 years, with falls of the order of 17% and 14% of the GDP in 1974 and 1982, reaching historical peaks of recorded unemployment in 1982 and of economic inequality in 1987 (Ffrench-Davis, 2014). Only an ideology fully rooted in the national consciousness could survive that.

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8.8. The ecological domain and the Privatization of Pool of Common Goods

The deterioration of the environment and the non-renewable stock of non-produced assets has produced a direct relationship between the ecological domain and the growth dynamics of the Chilean economy. The different ecosystems of the country have been the main source that has fuelled the processes of product growth. Energy centralization based on extractive projects, privatization and scarcity of water, the

transformation of the landscape of the regions, the destruction of biodiversity, the privatization of fishery resources, the externalization without private cost of pollution associated with industrial, agricultural and mining processes (especially those of the large copper mining) are a hidden face of the growth of the Chilean economy and have long explained the strength of the dynamic of high growth with very low productivity, exhibited by Chile. Each of these environmental elements has been enabled and maintained by a set of arrangements that have made up the institutions of governance of the environment, a domain in which bears the distinctive stamp of the Chilean model.

The Chilean natural resources sector presents a dramatic picture. The system of granting rights to private sectors over marine resources and water reserves (sectors in which resource exploitation has been both intensive and extensive) allows us to state that both resources can be considered almost completely privatised in Chile.

Neoliberal economists have designed and implemented granting private property rights as an adequate policy solution to promote conservation of natural resources (Fontaine, 1994), In terms of furthering privatization, the dictatorship is best known for the privatizations of water rights. However, post dictatorship governments have strongly promoted the privatisation of communal property and state land, sustaining which the objectives of that clearly neoliberal policies are aimed to increase protection and sustainable use of natural resources.

Their standard argument was that private property allows the internalisation of many of the external costs associated with communal ownership, because owners can appropriate all the benefits. They asses that this concentration of benefits and costs on owners can create incentives to utilise resources more efficiently.

The basic arrangements of this area were established during the dictatorship; however, their rules and characteristics were refined during the post dictatorship governments by means of the establishment of new institutional arrangements expressed in specific laws and complementary informal rules; a process that preserved the dominant position of large business groups who are now owners of the principal natural resources of the country.

The path to environmental convergence with developed countries it is a policy issue in which post-dictatorship are not focused. The severe environmental damages in

Chile made it necessary to make stronger environmental institutions, but actually the vague environmental policy has maintained their institutionality unfocused and without appropriate resources.

The fragility and manipulation of environmental impact assessments is a peculiar institutional feature of the Chilean model, and during the period under analysis there was no policy initiatives in that direction.

The same happened in issues related to quality and emission standards for air, water, waste and nature management. Additionally, Chile seriously lacks in the use of economic instruments oriented to territorial management policies, including national as well as regional plans and strategies. In general, it is clear that Chile does not have effective institutional arrangements to assure compliance. Also, it does not have integration of environmental concerns in regional and municipal decision about land use, at national and regional levels. And neither does it have enforcement institutions that can enforce that polluters pay for their negative externalities through the appropriate service fee charges (e.g. waste management, access to protected areas, consumption of natural resources), with due regard to social welfare. Lastly, Chile also does not have a national set of indicators to measure environmental performance with respect to domestic objectives and international commitments.

The neoliberal environmental policies seem to think that the best environmental protection institution is a weak institution, moving the existing institutions towards weakness and manipulability of local officials (Lira, 2017). In the environmental domain, the neoliberal policy engaged in a hard defence of the growth process, it has centred its efforts in avoiding any legislative initiative that changed the institutional status quo, oriented mainly to the improvement of the procedures to define private rights and then to determine an area of action for the state (Fontaine, op.cit).

The permanent building of public-private commissions and inter-ministerial working committees, during the period under analysis, generally had as a primary objective, to untie the knots and barriers to large investment projects. Such that environmental protection policies tended to be presented as an obstacle to growth that should be cleared away with some haste. The infinity of arrangements at the local level that allow the development of extractive activities and cause severe environmental damage, have stimulated one of the main axes of the social mobilization of the communities, which, over the years, have become particularly acute and violent.

8.9. Conclusions

The unfinished Chilean transition from dictatorship to democracy shows clearly that the project of the military dictatorship and their neoliberal advisors did not consist only in the creation of major rules of the game at the macroeconomic level.[280]

The Chilean dictatorship (1973-1989) was highly successful in the building process of institutional structures in which, within a neoliberal institutional environment, formal and informal macro and micro rules, enforcement mechanisms, governance mechanisms and preferences and attributes of the actors, were articulated.

The impact of that comprehensive set of institutions of governance which (at least for the purposes of our period of analysis) during 35 years (1974-2009) has been ensuring the sustainability of actions carried out by neoliberalism in the economic field, have articulated an intense neoliberal cultural identity of more affluent social segments of Chilean population.

The idea that individuals are only "rational homo economicus", oriented to prefer their interests and maximize their benefits. The conviction that the best way to satisfy the public interest is by allowing everyone to freely pursue their private interests. The idea that the economy includes all human activity, in such a way that there will be no actions outside that scope, because any action would ultimately be economic. The point of view that sees the bulk of human relations that seem alien to this logic, as mere accumulation of "social capital", or "cultural capital", has come to conform a body of ideas deeply embedded in common Chilean citizens and it has become the common sense of the elites.

Thus, a version 2.0 of Pinochet's speech against politics and politicians has been re-installed. The primacy of the economy is now maintained over politics and the market over democracy, understanding democratic institutions as entities that must have a

280 Features of that process also show that we are not in the presence of a uniquely Chilean phenomenon. Otherwise, we would be unable to explain why various elements of the Chilean experience are repeated in countries that, with a different historic context, also adopted neoliberal institutions. This last point is particularly relevant in those places who built institutions, with some neoliberal features, after the ending of their own dictatorships (such as Brazil, Peru, Uruguay or Argentina), or which presented similar trends of institutional capture by business groups within semi-democratic contexts, as occurred in Colombia and Mexico, or even in a fully democratic context, as in Costa Rica.

self-regulated nature and refractory to the interference of democratically elected political authority, that increasingly has been tinged with a halo of corruption.

The hostility towards collective labour rights and the transfer to the private sector of public functions that include the management of hospitals, prisons, roads and airports has been coupled with the massive transfer of property and public assets to the private sector.

On the other hand, the recursion of economic activities entrapped on a neoliberal institutional environment area nor necessary a by-product of neoliberal cultural devices operation. They are conditioned by institutional arrangements of the same orientation, that have influenced the scope of decision-making process of resources allocation. That process of decision making of Chilean economic actors has been framed in a logic of individual decisions, limited by institutional arrangements marked by neo-liberal logic. That state of affairs has produced a sense of belonging, inclusion trough consumption or when less of naturalization or neoliberal order, within segments of society that not can be defined as privileged.

This task was realised in such a rigorous way that the economic rules of the economic game established by Pinochet, remained essentially untouched more than 27 years after the end of dictatorship, being, after 1990, not only defended by supporters of the dictatorship, but also by some its former detractors, who have installed the bulk of the arrangements that sustain the neoliberal governance.

At the core of the decision not to amend the essential bases of the neoliberal model a series of arguments were raised and a multitude of factors came into play.

1. The solid economic growth showed by the Chilean economy during the first decade of post-dictatorship governments.
2. The lack of self-confidence of the new governments in their capacity to lead the country under the sword of Damocles of armed forces operating as an autonomous power under the former dictator (1990-1998).
3. The situation of the countries, neighbours in which new government´s poor economic management, eroded both the bases of economic growth as the new democratic institutions.
4. The unrestricted political and economic power of thirty business groups that produced in 1990, close to 80% of GDP, maintained a strong control of the

media, gave unalterable support to the neoliberal model of development and possessed the ability to capture the project of its political adversaries and even to a part no less than its leadership.

The first three factors had disappeared by the end of the last century, however, the fourth factor, linked to the "numantine" defense of institutional environment developed by the major business groups, had already become in those years the basic support of the neoliberal model, and that area was not boarded by the post-dictatorship governments.

The Political strategy of the business groups, oriented to defend their positions in the economic area, consolidated a dynamic that permits that non-market of activities of corporations may influence institutional mechanisms in a more powerfully than the will of the people expressed in free elections process.

Political devices, such as the binominal electoral system existing in Chile, have positioned the institutional environment as an almost impregnable barrier to the expression of the will of the people in the political system, avoiding mayor changes in the economic area.
The financing of political activities carried out by the large economic groups (in a way both legal and illegal) has completed a picture of semi-sovereign and limited democracy that characterized the Chilean political life.

In Summary:

- The Chilean experience shows that commitments with actions tending to promote institutional quality, such as the stimulation of competitive markets, anti-trust law enforcement or consumer protection, should not be taken for granted or considered as an automatic outcome of an open and liberalized economy. The setting up of institutions of economic governance that granted to the various social and economic actors equal rights, symmetrical rules of the game and similar responsibilities in relation to these institutions, has not been, nor much less, a product that could be associated to the process of neoliberal reforms implemented in Chile.
- Within regimes, as the Chilean one, that are only formally democratic, any progressive economic change would be highly conditioned in their performance by the presence of neoliberal-political-institutions. Additionally, any change to the rules of the game depends on the presence of the serious will of its current administrators to change these rules, or on the ability of subordinate social

actors to force them to try to exceed the neoliberal boundaries of that rules. However, in Chile, at least since 2009, there is more evidence of neoliberal rules of the game changing the performance agents, than evidence of actions of these agents confronting the neoliberal rules of the economic game, acting by themselves or under social pressure coming from the streets.[281]

- Neoliberalism has often argued that an important role of the democratic political system, must be to restrict the ruler's capacity to make bad institutional choices. Based in that approach, in a context like the Chilean one, in which the democratic system present serious limitations, the neoliberal business groups have identified almost any action of the post dictatorship governments as oriented by bad institutional choices. The presence of oligopoly markets and of underground control of the political mechanisms, has made possible the presence of institutional traps that, consolidated by the action of incumbent business groups that defend their corporate interest, it has caused the maintenance of low-quality institutions, characterised by high levels of capture. The Chilean neo-liberal order, as it has been described and analysed in successive chapters of this thesis, is characterized by their unequal access to the economic resources. Over this basic inequality, has been built a solid fabric of unequal access to social networks, and information. This unbalanced access to these factors is the basis on which asymmetric power´s distribution has been built and amplified.
- This process has led to the construction and consolidation of already mentioned institutional traps. After an initial a moderate effort oriented to improve income distribution (1990 1994), the Chilean economy entered a period which freezing the regressive distribution of income and limited any initiative to modify political institutions. Without the possibility of incorporating political changes, the bias incorporated on the neoliberal-economic-institutions was armoured. Given that political reality, changes to the core of economic institutional rules become almost impossible and only the modification of accessory elements to those rules were accepted by the new elites.
- The pro-wealthy economic bias of the Chilean economy was consolidated during the 90s. Firms and households were compelled to take their individual allocation and productive investment decisions within a clearly neoliberal institutional framework. By these means, an asymmetric level of influence of wealthy segments of population were established over society by the most

281 The irruption of the student´s movement of the year 2006, initiated a process of that nature, but that was quickly co-opted from the State. Ten years later the situation was different, but the analysis after 2009 is outside the scope of our research

powerful economic actors, consolidating their role as rent seekers which capture the political authorities during the period 1990-2009 and after. Because of that, there was often the presence of only a verbal commitment to institutional quality in Chilean political society, which included promises of changes to the actual institutional framework which were not maintained. The households and individuals who made decisions began to take as given the low quality of political decisions in regard to institutional quality (a process of learned-hopeless). All these contribute to a further consolidation of a kind of "common sense" that assume the form of a "neoliberal-culture" incorporated into the social fabric.

- The reorganization of culture producing institutions initiated by the dictatorship (e.g. universities, research centres, media, cultural industries, etc.) has produced a reconversion of the ruling-class' intellectual elite. It has allowed the decline of their social and economic influence over the social segments most disadvantaged, placing them in the hands of the economically dominant social segments, a phat that is now a defining feature of the economy in Chilean society. All that is allowing the dominant business groups to develop their coercive and hegemonic capabilities over the country. The deepness of that phenomenon has reached such relevance given that, an important segment of the new elite in the Government has been captured by neo-liberal thought and their economic power, inhibiting their possibilities of exerting some counter-cultural role to the hegemony of these sectors.
- Given dominance of neoliberal institutions (that cannot be defined as efficient institutions), the permanence of the neoliberal institutions has become an institutional trap that prevents an authentic development process. Thus, the aforementioned dynamics of "untouchability" of neoliberal institutional economic status quo, not only rest on actors´ micro decisions, but also upon opacity of development strategies defined at the highest political level. This dynamic is very clear if we observe that, in a short period, the post dictatorship governments started to promote economic concentration, allowing the development of a wide wave of mergers and acquisitions in sensitive sectors for the citizenry, such as banking, telecommunications and retail.
- The lack of clarity of the new ruling political coalition concerning the desirable features of the development strategy required by the country, has allowed neoliberal thinking to permeate their ranks. This situation is reflected in their absorption of part of this point of view on issues such as the State´s role, the desirable level of market competition and the mechanisms of power

decentralisation. Thus, instead of affirming the State's role in the development process after 1990, the Chilean centre-left wing elite tended to assimilate their formulations to the neoliberal model of privatisation and the subsidiary role of the State.

- That has been the source of a State penetrated by corporate interests, avoiding the evolution of greater social participation and increasing the centralisation process without the deployment of a deep State reform. This situation has produced a heavy restriction in the efforts towards making the Chilean political system more participatory and modern, a pre-condition for the improvement of the state´s ability to foster systemic competitiveness.
- In general, post dictatorship governments were notorious for being amalgamated in many ways (not all of course) to the neoliberal conceptual framework that had been guiding the Chilean process of economic openness from 1973 to now. In such approach, it is assumed that if the economies develop a trade openness process, then foreign investment, technological progress, and even the distribution of income will tend to evolve progressively and converge towards a compatible balance with the desired dynamics of development, creating convergence with more developed countries. Given that, the growing economic power of business groups appears as a secondary variable whose erosion clearly was not a political priority. For that reason, this power was not being identified as undesirable; the disproportionate control of some large economics actors, or their political agents, over the decision-making process, for long time has not been considered as a relevant issue, even though for the common people it was clear that this issue affected the operation of the Chilean economy in almost every dimension.
- In Chile, the economic power of large business groups described in this chapter, is not subject to significant levels of competition and reduces the levels of general economic efficiency, either increasing price levels or generating a decline at the level of GDP, to sub-optimal ranks. This context thus generates a consolidation of practices tending to move the economy far away from the competitive context that neoclassical economics considers to be desirable. The presence of unequal levels of power in the process of decision-making exerts a large influence on the general development process. This institutional trap generates a political bias coupled with income inequality, and from here, a political process is created which is unable to define the degree of institutional quality that would avoid the propensity of large economic actors to engage themselves in wasteful rent seeking activities.

- The information and analysis of the Chilean economy contained in this research is not the only evidence available on this matter. In fact, there is multiple local evidence (some of them reported throughout the different chapters of this dissertation) and substantial evidence worldwide, that institutions may cause development or, on the contrary, act as a barrier to it and so generating the formerly described institutional traps. Our analysis of the Chilean case shows that traps that has materialised the extremely powerful automation of the kind of economic relations promoted by neoliberalism. It allows the public to visualise the progress of the daily economic order, independently of the origins of that order, generating a not insignificant cultural force in favour of the status quo. This process hides social and political forces behind institutional structures, whose origins tend to be forgotten with the passage of time. Nevertheless, it is frequently observed that some authors point to Chile as example of one of the strongest institutional fabrics of Latin America, in the approach adopted here we are not using the same distinctions as these authors. When they refer to the strength of certain Chilean rules of the game, we are thinking of the weakness of other institutions that are the more important ones, in our opinion.
- The presence in Chile of property rights and legal guarantees to foreign investment and large business groups, a judicial system that has low levels of corruption (when punishing minor crimes) and in general the low presence of discretionary decisions by authorities, makes a positive difference when the country is compared to most countries of Latin America. However, the biased evaluation of presence of those factors neglects the nothingness of a solid antitrust law, the avoidance of predatory business practices, and the absence of a real democratic institutions or a transparent political and legislative system.
- The verticality and centralism of the executive power, which, within other factors, has been translated in a hard-metropolitan concentration of power and decisions, has ended up forming a key factor associated to the Chilean deficient institutional environment.
- Analysts that explore those facts generally stress that having emerged from a highly discretionary dictatorship; Chile is in a favourable situation in comparison to many democratic countries of Latin America. However, when we consider institutional development, the relevant question is whether the prevailing rules of the game are or are not appropriate to move Chile forward on a path of i) diffusion of technical progress ii) growth iii) income redistribution and iv) an inclusive political system.

- Obviously, it would be possible to install new rules of the game in Chile to achieve these three objectives. It would require actions, priorities and strategies very different to the rules that ensure the profitability of foreign investment, or which allows large business groups may control the oligopolistic Chilean markets. So that despite, from the point of view of large corporations, Chile is an outstanding example of institutional strength, from the point of view of its development goals, it is obvious that the country has weak and precarious institutions.
- Chilean experience finally shows that the implementation of reforms such as trade openness, has been unable to help by itself the country to escape from the trap produced by institutional weakness that characterize the country
- Such weakness prevents reform of the extractive dynamics which have characterized the Chilean economy and allowed it to garner a positive reputation based on its GDP growth dynamic. Because that, Chile has not been able to gradually move towards an inclusive and democratic economic dynamic, forsaking their originally proposed "equitable growth" goals.

Chapter 9

Final Conclusions

The objective of this last chapter is to present a summary of the main findings and conclusions of our study, which we hope will enable a new perspective for evaluation of the achievements and failures of the Chilean development model.

That is not an easy task, because this evaluation is a sensitive issue for a country as Chile, which, during the analysed period, has been implementing a neoliberal development strategy which, has declared to be the only route to obtain the growth and distribution goals to which its society aspires.

The implementation of a radically neoliberal development model, such as the Chilean one, given its historical origins and the role played by it in the international debate regarding the selection of appropriate policies for the developing countries, has produced two big groups of interpretations. For some, scholars and international organizations, the implementation of Chilean Model has been a case in point of undoubted success. On the other hand, for other people and academic entities, the Chilean reform process that allowed the consolidation of the neoliberal model, was a resounding failure.

Our vision is in same way close to the second group of interpretations, even when we never assumed in our research an optics that would make us choose between absolute failure and the total success of the Chilean model. Our position was rather to investigate to what extent those promises of the model that the neoliberal thought indissolubly associated with the success of their proposals.

In our methodologic proposal, if it is shown that the promises of the Chilean model were not fulfilled (without exogenous variables explaining this failure), the neoliberal model implemented in the country could be considered a failure. That be true without it being strictly necessary to delve into the veracity of the model, analysing each one of the hypotheses of causality that should have explained this success. On the contrary, if the promises of the Chilean model proved to have been really fulfilled, would be demonstrated that the application of neoliberal policies would have been associated to the consecution of the promised successes, or at least not be an obstacle to their

achievements, in the event that exogenous causes were not those who defined the success of the Chilean experience.

For that reason, although we think that the Chilean model is so far from being the success that some analyst declares it is, our research was not focused in to define of a success or failure by mean of a testing process of the multiples relationship between explicative variables and policy outcomes. On the contrary, our focus was placed on the analysis of whether the model's achievements had actually been achieved or not.

For this reason, we proceeded in first place, to accomplish a long process of obtaining adequate figures that would allow to extract valid conclusions; a task that, given the low quality of the figures available in Chile, was not always easy. A second task consisted in crossing information coming from different areas of analysis in order to provide a comprehensive view of the referred outcomes. On that basis, our focus was on defining whether the successes of the Chilean model are genuine indeed. In other words, if the authentic outcomes of trade liberalization truly corresponded to the extraordinary results predicted by neoliberalism.

Therefore, our goal in this research was to analyse, in a critical way, the performance of the Chilean economy and the neoliberal model of development installed in this country. In order to accomplish that exercise, we used the following research hypothesis:

"Chilean economic trade openness and market liberalisation made it possible for the Chilean economy, from 1973 onwards, to equip itself with an adequate macroeconomic environment and a pricing mechanism that ensured an efficient resource allocation mechanism. As a result, the Chilean economy produced a reallocation of its factors of production (capital and labour), from its most backward toward the more productive and globalised sectors. Because of this, labour was relocated towards sectors of higher productivity, witnessed greater remuneration, in turn improving domestic income distribution, the market competition and the competitiveness of its economy. This allowed the country to generate growth rates that led it to converge, both at the level of its GDP and productivity, with the more developed economies, especially those belonging to the OECD, to which Chile was incorporated in January 2010".

9.1. The Falsification of Neoliberal Hypothesis

The process of falsification of this hypothesis was performed through the deconstruction of its six main components, which constituted six different, but interconnected, research areas. Together, they account for all of the constituent aspects of the neo-liberal hypothesis, which as has been described previously, was made explicit by prominent Chilean scholars and politicians ascribed to the neoliberal field. Additionally, similar hypothesis has been validated in several of its aspects, by the IMF, the WB and other similar multilateral financing entities:

1. Our first research area was focused on outcomes of trade openness and market liberalisation in the areas of the development of competitiveness, sectorial specialisation, export orientation and the dynamic of employment generation of different sizes of companies in the Chilean economy. In relation to this research area, findings obtained in the course of our investigation and reported at Chapter III, let us conclude that:

    - After forty years of trade openness and market liberalization, the sectorial specialisation of the Chilean economy continued unabated. The export orientation of the economy continued to be led by mining exports (56% in 1990, 58% in 2009) and by other primary-commodities exported in a very similar proportion to before the trade openness. The incorporation of non-traditional exports to the export basket has not been significant and Chilean companies export orientation has remained extremely weak.
    - Trade openness has clearly not fostered market competition or economic competitiveness. Chilean markets tend to concentrate more and more drastically, the diversification of the economy continues to be very low compared to the level of the GDP of the country and the competitiveness of the economy rests only on low value-added commodities.
    - The employment creation has been moving from MSME to LSE, by increasing the LSE participation in the generation of total employment (formal and informal) from 19% in 1990 to 33% in 2009. That displacement has not been translated into higher remunerations. On the contrary, it has been used as a means of rent seeking by LSE.
    - The presence of institutions of governance of labour markets, pushing down wages for small businesses, has consolidated the presence of low levels of MSME wages-ceiling which, are the base condition that

enables presence of low remunerations at the LSE Those institutions have consolidated mechanisms which, have reallocate resources from smaller businesses towards larger ones and from labour to capital, forcing reduction in MSME´s wages and so, allowing LSE to hire labour more cheaply than in a competition context.

- Those institutions of governance of labour markets are one of the variables that have significantly influenced the low impact of trade liberalisation on the income distribution and levels of poverty and inequality in Chilean society.
- A second variable and perhaps the more important one, is the presence of institutional arrangements, framed in neoliberal criteria, that regulate relationships among LSE and the remaining enterprises in the economy. Those arrangements impose institutionalisation of hard and asymmetric relations between differently sized firms, consolidating an unfair business model widely applied by LSE.
- That predatory model represents a specific and comprehensive modality of institutional governance, clearly harmful to the improvement of economic performance and to fair income distribution. However, it is highly functional to deepen the Chilean extractive model of development and to consolidate the disproportionate power of large business groups.
- This business model, embodied in the Chilean model of institutional governance, enforces several advantages for LSE: high reservation value, high profits and high possibility of prices and quality manipulation. Because of consolidation of the neoliberal market´s governance, both Chilean enterprises´ intermediate consumption as final demand of the institutional agents (households, government and others), has been concentrated by a small group of LSEs. This factor generates a powerful force that feeds iteratively economic concentration, but has the misleading appearance of being an automatic and natural phenomenon in the economy.

2. Our second area of research was focused on the effects of trade liberalization, and macroeconomic policies that complement it, on the convergence of the Chilean economy with mores developed economics. In relation to this research area, findings obtained in the course of our investigation, reported in Chapter IV, let us conclude that:

- After 40 year of trade openness, the effect of trade liberalisation, supported by the macroeconomic policies that complement it, has only produced a weak convergence of the Chilean economy with more developed economies.
- The target of full convergence of Chile with mores developed economics would be achieved, according to neoliberals and neoclassic economic theory, by a combination of macroeconomic equilibrium with changes in relative prices induced by trade openness and followed by a process of liberalising and resizing of the state role. This would automatically result in a better allocation of resources. However, this promised outcome of the Chilean model regarding convergence, has not been accomplished in forty years of openness, showing that the neoliberal model was unable to accomplish its forecasts and promises
- When we analyse data of period 1990-2009, it was not possible to reject the hypothesis that Chile is converging with the other OECD member countries in terms of product or in productivity. However, convergence tendency is extremely weak and fluctuating. Indeed, some degree of convergence should take place, as a tendency, when the Chilean economy grows more than the average of OECD countries. That situation occurred, during 1990-1998, which is part of the golden period of the Chilean economy, however after that, convergence tends to disappear and is only observed because the regressions employed consider a 20-year period, during which at least 8 of them, Chile stood among the countries of biggest growth in the planet.
- Forecasting this convergence tendency in the long run is only plausible if GDP and productivity growth remains similar to that which was registered during the golden period, and may be assumed as an invariable tendency for at least one or two additional decades. Nevertheless, given that from 1997 onwards both processes lose energy, the convergence tendency has diluted its initial impulse. TFP and APL tend to be stagnant, despite the presence of periods of high economic growth. If the economy is growing without an improvement in productivity, the growth process must be related to the extensive use of pre-existing resources or productive factors, and not due to the increased creation of added value, encouraged by trade openness and liberalisation
- The extent and speed of the convergence process of Chilean economy is not enough to fulfil the neoliberal prediction, moreover, it is possible to conclude that real convergence would only be possible about a century after the onset of the liberalisation process.

3. The third area of research was focused on the effects exerted by on the diffusion of technological progress in the Chilean productive fabric. In relation to this research area, findings obtained in the course of our investigation, reported at Chapter V, lets us conclude that:

- If trade openness, market liberalisation and their by-product (the increase in FDI attraction capabilities), have not been able to produce a significant process of technical progress diffusion, we can only conclude that the liberalisation process is highly disconnected from the process of resource allocation. Given that, it has been unable to transform the Chilean economy, at least not in the sense that the neoliberal model had proposed.
- The lack of diffusion of technological progress in the Chilean economy does not seem to be an issue linked to the extent of the trade openness process or market liberalisation process. On the contrary, it appears to be more strongly related to institutional problems that distort the positive effects of trade openness and market liberalisation, independently of the extent of these processes.
- The institutions of governance associated with the Chilean neoliberal model, from 1990 to now, have defined the manner in which power is exercised in the process of resource allocation and also delineated modalities of coordination and control currently in use in the different markets of the Chilean economy. The neoliberal institutions, from the outset of the model's implementation, have been playing a critical role, determining the economic performance of the economy as a whole, more through institutions rather than through free market operation.
- Governance of the various domestic markets, built during the process of openness and liberalization of Chilean economy, cannot be defined as "good governance". Their orientations are not aimed at the reduction of transaction costs existing in each market, but rather to the expansion and consolidation of the market power of large companies that have come to dominate the country's economic life. As a result, an excessive increase in the market power of large companies can be observed, which has produced a worsening of the market allocation efficiency, reducing competition by means of reduction of market share of any other enterprise that defy market power of the LSE. This dynamic has maintained depressed labour remunerations, favoured the adoption of low productivity labour-intensive technologies within the LSE sector, weakening the growth capabilities of the Chilean economy as a whole.

- This particular model of governance is the source of the LSE's vertical control of the markets and of the great market power that they have accumulated. This phenomenon of centralized control and accumulation has produced serious difficulties in the dissemination of technological progress and also has induced severe difficulties, sector-to-sector, in the field of chain upgrading. The absence of the concerned upgrading has had a negative influence on the operation of productive chains, influence that has been transmitted to the economic sectors of which these chains are part and from that sectors, to the economy as a whole, being its most conspicuous expression of that issue the stagnation and fall of multifactor productivity in the Chilean economy.

4. The fourth area of research was focused on the effects on productivity payoffs arising from trade openness and market liberalisation, the quality of the country's institutions; the relationships existing between the effectiveness of antitrust policies and the promotion of innovation and total factor productivity. In relation to this research area, findings obtained over the course of our investigation and reported at Chapter V, let us conclude that:

- The effects on productivity payoffs arising from trade openness and the market liberalisation of the economy, are highly conditioned by the bad quality of the country's institutions. This is especially evident in the area of the relationships existing between the low effectiveness of antitrust policies and the weak promotion of innovation and productivity growth.
- The lack of a relationship between openness and productivity contradicts the neoliberal hypothesis which sustained that there would be mayor payoffs in the growth process from these two strategies. However, if the Chilean economy is growing and there is no significant productivity pay offs, the core of neoliberal proposals must be considered as falsified.
- However, efficiency, organization and innovation are key dimensions of competitiveness; development of those factors of competitiveness does not seem to be solidly installed in the Chilean economy.
- The bulk of the large Chilean companies are not part of global processes of innovation and competitive development. These companies operate mainly in domestic markets (mining, real state, utilities (gas, water and electricity), fisheries, cellulose, retail and are not subject to higher levels of competition from the global economy and locally in general is observable that around three or four large firms exert the control of each market of the Chilean economy.

- The unique market challenges faced by these large incumbent companies comes from the precarious MSME sector, which is, however, treated by business groups with all the hardness that institutions allow them.
- The country's institutions clearly do not comply with the quality standards appropriate to ensure efficient market performance. This has resulted in a vicious circle in terms of the relationship between openness and productivity, enforced by the low effectiveness of antitrust policies, producing low levels of innovation and total factor productivity in the Chilean economy.

5. The fifth area of research was focused on the effects of trade liberalisation on the growth process, income distribution and levels of poverty and inequality. In relation to this research area, findings obtained in the course of our investigation and reported at Chapter VI, let us conclude that:

- The Chilean economy, as a result of its trade openness, experienced a strong period of economic growth for slightly over a decade (1987-1997), which came to an end during the Asian crisis of 1996-1998. Following that crisis, the economic growth of the country declined steadily.
- There is no evidence that this growth was due to greater efficiency in the use of resources, induced by trade liberalisation, even during the golden period. During that decade, only between 1991 and 1997 the TFP increased at the aggregate level, however the bulk of the growth, as has been reported, was supported by the extensive use of productive factors rather than on the productivity of these. Conversely, there was abundant evidence to show that this growth was a result of an increase in exports from the primary sector, in which the country has traditionally specialised, as well as the extensive use of cheap labour and natural resources of the country.
- In terms of social aspects, it was visible that lowering GDP growth, during some years, was the source of changes in the distribution of incomes of people and families, and stemming from that circumstance, changes in the proportion of the Chilean population living under the poverty line. For that reason, despite the fact that in some years of the analysed period changes to the number people under the poverty line seem to be a consequence of growth that does not affect inequality, because the causal relationship among these variables shows to be more complex.
- The Chilean process of economic growth has not been able to reduce poverty in the way that was promised by the supporters of Chilean model. On the

contrary, the Chilean economy is showing increasingly less capacity to produce serious reductions in poverty through economic growth that exerts a moderate-to-low level of incidence on the poverty reduction.

- Contrary to the neoliberal hypothesis, in the Chilean economy, only has been made clear that economic growth reduces poverty significantly headcount only when GDP presents a very high growth rate, but that kind of poverty is not significantly reduced if those outstanding rates are not present. If in the next half-century, Chile does not achieve similar rates to the golden period; achieving full poverty eradication will become an unrealistic goal.

6. The sixth area of research was focused on the analysis of setting up and upgrading of the institutional environment and institutional arrangements established during the 1980s and consolidated during the 1990s, which define the real impact of trade openness and market liberalization over the Chilean economy. In relation to this research area, findings obtained in the course of our investigation and reported at Chapter VII, let us conclude that:

- The Chile´s neoliberal institutions were created by a set of voluntary actions, implemented by the most powerful economic and political actors of Chilean society. These institutions were designed by a group of extreme-right wing scholars, supported by the military power emerging from a bloody coup de état. They had the prerogative to take unilateral decisions, not submitted to any multi-agent negotiation process regarding the institutions to be created.
- The members of the neoliberal groups emerging after the coup, built institutions granted of a self-enforcing character, in order to prevent conflicts that can emerge when the interest of dominant groups and subordinated groups do not coincide. The unrestricted power of dictatorship was the tool utilized by them in order to implement their institutional model.
- The establishment of the new institutional environment and new institutions of governance during the eighties was the variable which has defined the real impact of trade openness and market liberalisation.
- The "free" operation of the price system associated with trade liberalisation, have failed to impose the force of such price system, over the market governance institutions. If price system is understood as the means by which each single market activity is controlled or directed, findings of this research are clear about the supremacy of institutions of governance over the influence of prices induced by trade openness.

- The Institutional arrangements that predominate within goods, services and labour markets; are those that define the opportunities that the neoliberal model has offered to different economic agents, reducing through that mechanism the possibilities for poverty elimination, inequality reduction and the building of an economy which produce aggregate value, all of them outcomes promised by neoliberal when they start installation of the Chilean model.

In sum, in the course of this research, we have demonstrated that in a full open economy such as Chile's, trade openness by itself is not enough to promote significant improvements in competitiveness and productivity. In addition, maintaining a pro-market orientation, achieving a certain macroeconomic balance, and driving some institutional macro reforms, is not enough to achieve a genuine development process.

The findings, reported in the different chapters of this dissertation, lets conclude that the core of the neoliberal hypothesis may be considered falsified, giving the abundant evidence supporting the conclusion that the outcomes of the process of opening and liberalization have not been achieved in the way that the neoliberal model had promised. There is a lot of evidence reported in this research that, additionally suggests as a highly plausible hypothesis that, in the Chilean economy, there is a greater influence of institutional factors than of the price changes induced by trade openness.

We report evidence that shows that, from 1990 onwards, trade openness and market liberalisation did not allow the Chilean economy to equip itself with adequate institutions of governance. Perhaps the public budget has been managed responsibly and the national accounts show goods indicators, but these elements have not been enough to allow to the Chilean economy to be capable to adequately deal with its development process. We also demonstrate that a pricing mechanism that would ensure an efficient resource allocation mechanism has not been introduced. Without the presence of this kind of price system, the neoliberal project lacks firm foundations.

9.2. Outcomes of Neoliberal Proposal about "Resource Allocation based on Right Prices"

Given that trade openness has failed to introduce a system of "right prices", because it is difficult to sustain that the Chilean economy produced a massive reallocation of

their factors of production (capital and labour), from its most backward toward the more productive and globalised sectors.

An appropriate reallocation of resources based on market mechanisms, requires that prices of various production factors be correlated to productivity, and in turn, be correlated with their relative scarcity. However, if the remunerations of the main factors of production, capital and labour, are not determined on such basis, it is highly unlikely that both factors may be properly allocated in the economy.

The data provided in the course of this investigation shows how productivity does not increase remunerations. Productivity is much higher in large Chilean companies that are only 1.3% of the total formal enterprises. On the other hand, in the remaining 98.7%, productivity is very low. However, in that research has been displayed which, the wage differentials between small and large companies are not particularly significant, because wage levels only differ in 25% to 30% between large and small enterprises.

This situation has produced a significant rent capture for large companies, which absorb the differences existing between the high value of marginal product produced and the low wages paid to workers that generate that value.

In summary, liberalization had a positive effect on economic growth during those periods in which, the trends of the world economy and the price of commodities exported by Chilean economy allowed. However, that impact was weak and intermittent, producing little more than a decade of high levels of growth, which stalled when it was necessary to incorporate higher levels of productivity and added value to Chilean exports.

9.3. The Extractive Sign of the Chilean Model

The neo-liberal model of development built in Chile has an eminently "extractive" character; in the stile which it concept was devised by Acemoglu and Robinson (op. cit.), e.g. extracting incomes and wealth from a subset of society to benefit a different subset. Outcomes of the Chilean model show that the country's export strategy as promoted by neoliberalism, was based on the natural resource exports, but did not lead to higher multifactor productivity and that the hoped presence of technological spill overs and linkages did not happen automatically or did not happen at all.

If we evaluate the way in which Chilean neoliberals manage the weak evolution of TFP aspects of the economy, it is clear what, within the imaginary of the neoliberal-extractive model of development, that is not a crucial issue. On the other hand, for the neoliberal proposal, build the sustainability of GDP growth process based on a productivity growth dynamic, is not visualized as a vital problem. They seem to believe that, the firm's capability depends essentially on their endogenous characteristics and on its reaction speed to changes on relative prices. Nevertheless, contrary to that belief, performance of Chilean firms in the growth area, is strongly conditioned by the institutional context in which they operate.

If that institutional context favours a regressive distribution of wealth, from the poor to the owners of resources to be extracted, there will be no pressure, from the incumbent groups, to change the institution's status quo, nor to sequentially introduce transformation of productivity development strategies.

Quite the opposite of the neoliberal view, openness and free market reforms were not part of a specific institutional environment whose outcomes are predetermined by the general design of openness process. On the contrary, such outcomes are heavily dependent on the historical, political and social characteristics which that environment could assume in each singular national context. In some cases, it may favour to extractive strategies or, as it also can, in other cases, be a catalyst for a development model inclusive and centred on the increase of the generation of added value for the market.

If it is estimated that the opening and liberalization of markets, cannot but produce a new price system based on the absence or minimization of state regulation and thus endowed with an intrinsic allocation efficiency, the conclusion could not but be one: The price system is the heart of the institutional framework necessary for any economy and success will be assured if that institution operates as freely as possible, regardless of the environment and institutional arrangements within which it operates.

The Chilean case here analysed, shows that the free price system should not be considered as the key institution which by itself determines the whole institutional environment. The price system, in light of the Chilean case, seems to be just another institution, which, depending on its interaction with the rest of them, can enhance or degrade the process of resource allocation. Given this, an adequate development strategy should not be evaluated only in terms of the degree of openness and liberalization of its markets, but on base of the national capacity to ensure that both measures do not

feed the vicious circle of political structures which, do not constrain the use and abuse of power by the economic and social actors of greater relative power.

The Chilean trade openness is so far to constitute, "per se", a negative element for the Chilean economy. On the contrary, it has brought many positive elements and, in many areas (given the wide support received from the main political sectors), may be considered a path of no return. However, our impression is that the institutional building mechanisms that, supported on a neoliberal view, have accompanied these processes, have not been adequate because that does not tend to induce linkages between firms, sectors and social and economic actors, that would enhance productivity. In other words, the Chilean model ha consolidated exclusive and extractive institutions which, constrain the possibilities of the economy to move toward a more inclusive development model. On the contrary, their focus was placed on building an economic space that be highly excluding of the more vulnerable economic actors, but attractive to foreign investment and the domestic economic powers, even that space be unsustainable in a scenario of low prices of main exported commodities.

Chile shows a very high correlation between GDP growth and the cycle of the high prices of commodities, rather than to the evolution of neoliberal reforms that intended to establish a more efficient mechanism of resource allocation and productivity improvement, through changes in relative prices.

If in the Chilean economy, presence of high productivity and inclusive institutions are not the basis for economic growth, would be very difficult that changes in GDP level to be able to support some sort of sustainable convergence towards a similar GDP per capita level of some of the less developed OECD European countries.

Chile, as the best Latin American student of Washington Consensus, did not understand that their economic authorities needed to adopt a more activist position to overcome market and institutional failures in certain critical areas, and not only accept the subsidiary role which the recommendations of the Washington Consensus and the neoliberal approach prescribed. Quite the reverse, accepting recipes of WC, did not enhance competitiveness and GDP growth and consolidation of an extractive economic dynamic (mainly supported by natural resource exports with low levels of added value), was the real outcome of the Chilean model.

9.4. Institutional Traps

Basically, the presence of the so-called institutional traps, is an issue related to the lack of an adequate institutional development. That traps may be self-supported by several mechanisms. These are frequently observed in economic contexts in which predatory conducts dominate behaviour of some economic or social agents. That kind of practices are usually characterized by the rationing of divisible benefits on the basis of favouritism, and by off-market actions oriented to buy political support that favour some interest groups. Such pattern of economic conduct is more likely to result in much unproductive rent-seeking activity. Moreover, political forces controlling the state; could become hostage to these market activities which generally involve bribery and other illegal conducts very frequent in the Chilean context.

In general, it is clear that predatory institutions lead to economic stagnation, feeding the presence of institutional tramps. There are political and economic factors determining the presence of such conducts, which produces adverse effects over capital accumulation, political and economic institutions, international trade, and economic policies.

In general, traps frequently arise due to such institutional failures. In our research we show how, the process of capital accumulation may be very different depending on the dynamics that those traps may activate in the different socio-business groups of the country. A pattern of growth and accumulation based on an extractive model increases the likelihood that "inequality traps" will emerge. In this way, we show how in Chile the adverse effects of the inequality of income growth tend to reinforce the high concentration of ownership of production factors and incomes.

When such "traps" are avoided, abundant research shows how virtuous circles of fast growth and rapid equalisation of income arise, relying on manufacturing power, the accumulation of qualifications and the high growth of the productivity of the productive sectors. However, clearly that was not the Chilean case after the end of dictatorship.

Our analysis of the Chilean case shows that, to the extent that institutional traps have materialised, they generate an extremely powerful automation of economic relations. This happens at the level of the unequal generation of the added value of intercompany distribution processes, the biased orientation of consumption of households of different income levels and also the also biased consumption of Government and intermediate demand of differently sized companies in the export sector.

A core outcome of the neoliberal institutional framework has been the asymmetric relations established between economic agents of different sizes and market power. This has in turn consolidated, as a by-product, the unequal distribution of the capabilities of producing and distributing the produced added value between all those agents. In that context, inequalities are feeding an amalgamation of inequalities and asymmetries under the appearance of normalcy.

The institutional installation of this framework has been heavily guided by what neoliberalism conceives as desirable economic relationships, i.e. the superiority of an individualised market-based competition over other modes of economic organisation. However, in the Chilean case, this has not been the result of spontaneous evolution occurring because of human action. It is clear that it is an outcome of a neoliberal design imposed through violence and the control of political institutions.

9.5. Neoliberalism and Convergence

The presence of enduring convergence was not the one that neoliberals declared would be produced by the changes in the relative prices of the economy, delivered by trade openness and market liberalisation.

In the Chilean context, it is clear that the presence of entropic relationships amongst variables such as the raising GDP, the slow improvement of the political framework, high income inequality, a weak institutional quality and weak income redistribution. Chile demonstrates a model whereby a not fully democratic political process, the presence of neoliberal institutions and income inequality are negatively influencing the economic growth dynamic and possibilities of convergence.

The articulation of all these elements has been transforming the Chilean economic structure into one that is strongly and deeply extractive. Obviously, it would be possible to install new rules of the game in Chile that would lead the country towards a real convergence with developed countries, but it would require markedly different actions, priorities and strategies to the existing rules originally installed by neoliberals and later tolerated and promoted by post-dictatorship governments.

Nowadays, these rules only exist to ensure the profitability of large business groups that control the domestic and export markets. Nevertheless, they have not enforced

an inclusive and productive economic development path, nor produced the outcomes originally promised by the neoliberal model, as, for instance, a quick process of convergence to remaining OECD countries.

Our research shows that openness was, without a doubt, correlated with the process of economic growth and also with the Chilean institutional evolution. The central challenge to Chile is one of productivity, and its convergence with the more developed countries is dependent on the evolution of this variable. However, given that this challenge cannot be solved at the technological level, but only at the institutional one, successive democratic Governments from 1990 to 2009 have unfortunately tried to tackle these transformations following the institutional recommendations proposed by the Washington Consensus.

The results of this decision were disappointing; productivity did not increase but actually declined, GDP growth lost its former dynamism, inequalities increased or remained unchanged, and the hope for convergence was repeatedly postponed, without ever being realised. We have shown in the course of this thesis that whilst the growth of Chile has been weakly converging, over the long term, with OECD countries, this convergence requires very high rates of economic growth to be realised, and these seem to be a scenery increasingly elusive for the Chilean economy. The conclusion we have drawn is that the long-awaited convergence can only be assumed as a general trend. However, given its links to internal and external phenomena clearly misaligned with this objective, it is highly unlikely that this will occur over the course of this century.

9.6. Governance of Productivity and Spreading of Technical Progress

Productivity growth is not only a technological issue, nor can it be considered dependent only on institutional factors, being rather a result of a wide group of factors which interact in more complex and multifaceted ways than the neoliberal proposal suggests.

From this perspective, the neoliberal strategy of openness and liberalisation was expected to lead to higher productivity growth and GDP growth, associated with increased competitive pressures on domestic producers, greater domestic access to the international production processes and technologies that qualify as best practices, and

to a wide absorption of positive spill overs. However, these expected benefits did not appear because the appropriate institutional framework was not in place.

The Chilean experience analysed here shows that market liberalisation and trade openness do not generate economic and productivity growth if markets are not fully competitive and if there is not a suitable institutional structure endowed with an appropriate governance system. Without this device, the Chilean economy is not in a condition to share the created wealth amongst all economic and social actors. Instead, it reaches only a few business groups that control economic and political institutions.

The constraints to GDP growth, which Chile has been presenting from the beginning of this century, can be clearly attributed to a structural fall in the TFP and not to a low rate of the use of production factors. The figures provided in this research clearly show that Chile is following an extractive strategy of development, using an increasing volume of production factors to produce decreasing levels of product. This demonstrates that Chile is far from the technological frontier defined by the more developed countries. Despite the fact that the country displays significant progress with regards to the remaining countries of the Latin American region, its productivity gap with the world class technological frontier is, however, substantial.

The unilateral openness developed from 1976 to 1990, was followed by the subscription of many FTA that have been nominally expanding the access to markets that domestic firms potentially needed to expand their operations. Both neoliberal strategies were exhibited as a sensible way to expand the technological frontier and disseminate technological progress from the global markets to Chilean companies, specially LSE which were assumed would be firstly internationalised, later spilling over to smaller companies.

Nevertheless, in practical terms, only a few larger enterprises have taken advantage of these new possibilities. That means that market and technology access has tended to be monopolised by a group of firms with high market power. Industrial organization's governance and mechanism of technology spreading were not oriented by the system of relative prices induced by trade openness; on the contrary they were based on biased institutional arrangement slanted towards fostering of business concentration. Chain upgrading is not a feature of the Chilean economy, for that reason technical progress is not spreading on the productive fabric and productivity has been lost or decreased throughout the analysed period.

If Chile would proceed, for instance, to bridge its productivity gap with the USA, the country may eventually approach the USA GDP pc. in an affordable period of time. The growth of Chilean GDP pc would strongly react to a bigger elasticity education-productivity than existing in USA. This would occur despite the gap in the intensity of utilisation of workforce and the impediments to investment in physical capital, because, given its current high elasticity productivity-education, the Chilean labour force has a level of education higher than the USA has at the same level of primary incomes.

Higher productivity would allow Chile to not only use both physical and human capital more efficiently, but at the same time would also imply a faster accumulation of these factors of production, as a reaction to the higher profitability produced by a rise in productivity. This factor would allow the Chilean economy to provide a renewed impetus to the process of GDP growth, facilitating the closure of the productivity gap.

For a country like Chile, with unemployment rates close to 8%, with high rates of investment and high levels of investment attraction; the closure of productivity gap must be determined by on the development of national capabilities to obtain a raise in GDP using similar levels of productive factors. Nowadays, nevertheless the limitations to the dissemination of technological progress at the enterprise level exerts a heavy influence on aggregate productivity, it strongly depends on variables associated with the specific relationships launched between markets and the features of the institutions of economic governance prevailing in the Chilean society. Without addressing the increase in productivity from that perspective, it is seen as extremely difficult for the Chilean economy to obtain significant improvements in that area.

9.7. The Neoliberal Model Transform Predatory Business Practices in Institutions of Governance.

In Chile, the neoliberal proposal has become a contradictory corpus of ideas, composed by a discourse that advocates competition and free markets, but actually operates as a driver of the market power concentration, fostering oligopolistic markets. Given this, the impact of business models developed under the umbrella of neoliberal market governance institutions, has tended to be more important than the price-effects of trade openness, and hence reducing its impact.

Our findings show that contrary to neoliberal forecasts, the predatory activities associated with oligopolistic markets do not disappear with the arrival of trade openness, and therefore cannot be considered a transitory phenomenon, likely to disappear when openness has been fully achieved.

The complex and unequal arrangements that Chilean MSMEs face, have been reported in several articles and investigations, many of which have been cited in this dissertation and in several reports by the FNE, who have identified them as the most important problems of MSMEs and also as an important distortion of free market mechanisms. For instance, according to the report of the National Economic Attorney (FNE, 2007), in Chile currently there are variations of payment terms depending on the bargaining capacity of the suppliers, so that for large industrial suppliers (such as e.g. Procter & Gamble or Nestlé), immediate payment terms are established (one week), while for the MSME the terms can reach 120 days and more. In addition, there are frequent price discriminations based on purchasing volumes, a practice that (in the absence of differential costs) is expressly prohibited in many anti-trust legislations of the most developed economies.

These and other abusive practices that are part of the business model of large companies, are so numerous and important, that they put at risk the survival of the weakest companies, being possible given the presence of institutional arrangements that make them possible. Against the neoliberal opinion, many of the problems of the MSME do not seem to be attributable to inefficiencies of their operation, but to the abuse of a dominant position and the implementation of predatory practices by some of their large clients.

In the current Chilean economy, the biggest area of problems facing MSMEs area related to the business procedures imposed by their large clients. As has been reported in the previous chapters, in practically all sectors it is observed that, the higher the market concentration, the more adverse the negotiation conditions that small and medium suppliers must face, without mentioning that said practices would be more recurrent. That is why, when we use the term predatory to define a business model, we are not referring only to the presence of a predatory pricing policy, an issue otherwise widely discussed by the antitrust literature. We refer to the existence in Chile, on the part of the LSEs, of a large-scale use of their position and size as a tool of negotiation. Those practices constitute a pro concentration device that protect LSE from competition,

given that the market dominant position of that firms is so far from being limited by the institutional framework, on the contrary is encouraged by this.

Existing arrangements allow the LSE market share to grow through mergers, acquisitions, as well as the expulsion of competitors and generation of entry barriers as an absolute right of incumbent firms. In the same way, this kind of arrangements allow a drastic inequality in access to credit among different size of companies, a situation reinforced by the rules that facilitate the presence of oligopolistic capital markets, closed to competitive practices and characterized by high bargain's asymmetries between lenders and credit-seekers.

In Chile, after imposition of neoliberal model, there is no legal option to denounce the growing concentration of trading channels that has been generating a close integration between the activities of marketing and financing, promoting the concentration and subordination of trading channels to financing circuits. On the contrary, different institutional arrangements support the unrestricted maintenance of such business practices, understood from the neoliberal view, as a mere defence of "property rights", "economic freedom" and the "autonomy of private enterprise vis-à-vis the state".
The predatory business model, assumes the role of the dominant companies to be detached from any assumption of responsibility in relation to their stakeholders as a whole, understanding that they can conduct any kind of activities that the law established during dictatorship times does not explicitly disallow. Additionally, that business model includes a strong, yet not always legal, intromission of LSE into the parliamentary process of law-making, in order to legally avoid subjection to controls from the state authority. However, there is some kind of "bad conscience" in connection with this topic, on the part of the business and academic groups that promote the neoliberal approach.

Following the neoliberal reasoning, in the public declarations of the main Chilean large employer's organizations, LSE have acquired a large market power based solely on their efficiency. Then, from a crude Darwinian perspective, LSE domination is assumed by them as a "survival of the fittest", is worth to say, a victory of the "fittest" over the "inept", a situation which (for them), would only accrue benefits to the economy as a whole. But Neoliberal discourse, eludes, or hides, the fact that there are currently many parliamentarians and government officials who, together with high-ranking members of the main economic groups, have received substantial bribes to

approve laws or administrative ordinances that encourage expansion of the power of market of such business groups

The comprehensive character of neoliberal market arrangements that match up to the predominant business model in Chile, have led us to define it, as a predatory model, a situation that has been partially shared by the FNE (Resolution # 862 of the Preventive Commission) who defined a number of arrangements that are operating in Chile which give rise to doubts regarding their outcome. These arrangements include volume discounts that are not justified in the use of economies of scale in the production or marketing of products, or cases in which companies with high market share, systematically charge prices below costs, with the objective of scape from market competition. In each case, FNE is denoting predatory behaviours, operating through prices or other administrative mechanisms, which are unfair and detrimental to the economy and society.

That business model as a whole has consolidated institutions of market governance characterized by hard relationships between large and small size enterprises. As was reported in this research, the transferences of sales from LSE to SME from 1990 to 2009 are equivalent to more than 20 thousand million dollars, a figure equivalent to the "sovereign fund" in which Chile has inverted all the profits obtained by the higher prices of cooper during that period.

9.8. GDP Growth and Economic Concentration

As an explanation of the declination of GDP´s growth process, it has been argued that Chile's problem is that, having reached a high level of GDP throughout its period of faster growth, it is now a country with a medium-high income. Thus, it would not be reasonable to expect that its economy can maintain a level of growth characteristic of an emerging low-income economy, when it is in fact already an almost developed country. However, if we follow this reasoning, we must conclude that if such high rates of growth have not allowed Chile to converge with the levels of GDP per capita characteristic of a developed country during the golden period 1985-1997, in the future it would be hardly possible for the economy to grow at the levels required for convergence. Then, if that confluence of GDP per capita were not structurally achievable, it would scarcely be possible for the promised economic convergence to be feasible in the future.

As we have delineated previously, economic concentration in a small group of large companies who exert control over several different areas of the economy, such as banking, private health, export sector, supermarkets and retail, processed food, pharmaceutical sector and others, has reached unprecedented proportions. This situation, of clear institutional roots, generates higher incomes for these groups than in a competitive context like the Chilean one, worsening the already regressive income distribution.

The institutional variables have become relatively impervious to the processes of economic openness and liberalisation. Consecutively, this strongly limits the convergence of Chilean economy's productivity, which would aid in the reduction of both poverty and inequality. In Chile, the larger business group´s control over cash flow, consolidated governance structures in which an institutionalised economic structure makes it easier for larger incumbent firms to expropriate resources from other defiant firms. Hence, the potential social benefit of an increase in ownership concentration proposed by Chilean neoliberals, is balanced out by the presence of high social losses emerging from low productivity and oligopolistic market structures, affecting market competition.

In the Chilean economy, as has been reported in this dissertation, it seems clear that issues related to large ownership concentration, agency costs and resource expropriation, depress the process of domestic investment and productive improvement in a way highly related to the institutional structure in which the economy is developed.

Our analysis reveals other features that characterise the current stage of development in Chile as a process of open transition, whereby a set of internal and external determining factors from the political, economic, social and institutional realms are of key importance. Particularly important are those linked to the 1980 constitution, who made form and coherence to an institutional environment that frame to governance institutions who interacting with the authoritarian neoliberal-political-institutions that remain in the Chilean post-dictatorship, has allowed the survival in the country of the neoliberal model of economic development.

9.9. Regressive Income Distribution as a by-product of Governance Institutions

These weaknesses of Governance Institutions associated to the Chilean model produced problems not only in the economic area, they also produced very important social

issues relating to income distribution. That was empirically demonstrated in our research showing how Chilean social inequalities are largely explained by the impact of income concentration in the first quintile´s households. This regressive income distribution, at a household level, is rooted in the fact that the Chilean economy displays a strong concentration in the ownership of productive assets and its markets are not competitively structured.

We showed that despite the acceleration of economic growth in Chile over the last 25 years and the changes in its economic structure and long-term income distribution, the Chilean economy maintains high and persistent levels of inequality over time, reflecting the influence of long-standing structural factors.

We also showed how the period of economic reforms initiated by the military dictatorship in 1974 structurally transformed the institutional structure of the Chilean economy through external openness. The widespread use of market mechanisms in the resource allocation process associated with the reduction of the State role in economic activities, produced an increase in the levels of inequality that reached their peak in the mid-1980s. That dynamic could not be corrected during post dictatorship governments that only use as a policy tool, strengthening of trade openness and market liberalisation.

Thirdly, we showed how, although the strategy of the governments inaugurated in the 1990s was to reconcile economic growth with higher degrees of equity, levels of inequality in Chile continued be particularly elevated, whether measured by the Gini Coefficient or as proportions of the highest quintile and those that follow and/or the poorest.

9.10. The Economic Relationships between Sizes of Enterprises are an Expression of impotence of market prices as efficient tool of resource´s allocation

In this research, we used input-output matrixes disaggregated by size of company in order to visualise not only the way in which sectorial relationships are displayed in Chile, but also economic linkages between sizes of companies across sectors. From this analysis, the anomalous articulation of different company sizes within value chains was extremely clear. In addition, we could observe the degree to which this

dynamic has affected the performance of the Chilean economy and the achievement of its convergence goals.

The data provided by the Chile´s IOM disaggregated by size, clearly shows us how the bulk of national intermediate demand, which is produced by large companies, is geared towards products and services produced by companies of similar size and productivity. This not only happens in large enterprises oriented to the domestic market, but also in companies in the export sector. Thus, the effects of the commercial opening of the Chilean economy fail to permeate to the 98% of the economy comprised by MSME.

The weakness of linkages between different sizes of enterprises it has not occurred as a result of an automatic or involuntary process. On the contrary, it has been highly dependent on the institutional context that, in turn, has been dependent on the rules of the economic game introduced by a combination of policies inherited from the dictatorship and enlarged and strengthened by the new governments.

The reluctance to introduce new antitrust legislation, secondly, the promotion of a non- inherited governance system of market relationship between firms of different sizes, promoted by post-dictatorship authorities and thirdly, a wide group of business practices and administrative decisions that openly discriminate against MSME. All that, have greatly favoured the market´s concentration and dramatically reduced the market share of companies of smaller relative size and not subject to the control of large economic groups Additionally, the extent of the intermediate consumption and aggregate demand channelled to Chilean enterprises of larger size is an additional factor that has been heavily stimulated by the current institutional framework, that generally acts as a factor of market´s concentration.

The combination of these non-market ways of competition, shows the existence of powerful connections between the aforementioned weak economic linkages and the extreme concentration of economic power which puts more than 80% of the GDP in the hands of a small number of business groups.

Given all these factors, after scrutinising the Chilean economic framework, it becomes clear that the limitations to build a national economic dynamic characterized by competition and efficiency, have been linking to decreasing MSME market power and the most immediate consequences of this situation, the reduction of productivity and the declining MSME ability to generate quality employment.

9.11. The Institutional Environment after the Dictatorship Period

The Chilean Constitution of 1980 has been acting as safeguard to any institutional reversal, dysfunctional to neoliberal order, consolidating a dynamic that makes it possible for the non-market activities of large corporations, to influence institutional mechanisms more powerfully than the will of the people expressed through a free elections process.

Unfortunately, the Chilean centre-left governments (1990-2009) have failed to define new ways of confronting the institutional traps of the neoliberal model, which are almost impossible to tackle without incorporating into the economic activity new rules of the game, more democratic and inclusive.

During the analysed period, the main areas which the post-dictatorship governments boosted just nominally and that would have made possible eroded the bases of the neoliberal order, were mainly:

- Re-democratization of channels of representation of the interests of citizenship, currently in the hands of senior government officials and parliamentary leaders not subject to minimum standards of transparency
- Impulse to new forms of State interaction with civil society, that empower it beyond the hard limits that impose parliamentary structures that, although supposedly represent the popular will, in reality severely distort it, given the electoral norms inherited from the dictatorial period.
- New channels and structures of people´s participation at micro level.
- A new role of the political party system, democratizing their internal organization, forcing them to provide greater levels of internal transparency and institutionalized practices of accountability before citizens.

On the contrary, in all those areas, post-dictatorship governments have consolidated a very elitist institutional environment that fit perfectly with the neo-liberal perspective of exercise of power, given that all decisions concerning the condition of the lives of citizens and related to governance arrangements, have been concentred only in the small elites in charge of political power, without significant participation of civil society or empowered citizenship.

The problems linked to these areas, are particularly harmful because they constitute the natural space in which are placed the real possibilities to develop a broad coalition in favour of institutional changes. That is the basic condition necessary to overcome the neoliberal model. Without that progressive social, cultural and political movement, will not possible to deal with a real reform process, that might enable overcome the already quoted institutional traps.

Without overcoming these traps, which not only limit the deployment of distributive strategies, but also inhibit the growth process, would make it extremely difficult for Chile to converge with industrialised economies and democratize its society.

In Chile, in the economic field, the economic power of large corporations, which are not subject to significant levels of competition, is reducing the levels of general economic efficiency, increasing price levels to sub-optimal ranks, or generating a decline in the level of GDP to sub- optimal ranks.

From the orthodox neoliberal perspective, this phenomenon is not seen in the same way. From that perspective, it is argued that the fall of the GDP growth´s rate, is mainly linked to the presence in the government of political parties (centre-left) that do not generate confidence in the large business sector or in some foreign investors. Therefore, the fall in investment, the bad economic expectations of the big players and the regulatory measures (so timid, to tell the truth) that these governments have implemented, would be the cause of the stagnation of the Chilean economy. In other words, for neoliberalism, the fact that the Chilean economy has not maintained its past dynamism nor has achieved the expected objectives, lies in the role of the State and its policies.

However, this is a difficult point to defend, at least if we refer to the period under analysis (1990-2009), in which GDP growth was 5.18% per year, while between 1974 and 1989, growth was it was only 3.34%. The same happens with foreign investment which, during the period under study, reached the highest levels in the history of Chile, or with exports that behaved, quantitatively speaking, in the same way. Undoubtedly there are more empirical backgrounds around which to endorse our interpretation, than to value that of the neoliberals.

However, the criticism of the hardest neoliberal wing, towards the performance of the Chilean economy post dictatorship has been very hard. Especially the neoliberal

economists who occupied high post as public officers during dictatorship times seem to think that the main policy errors of period 1990-2009 are grounded in the fact that the non-neoliberal economists and the new political authorities, have assumed that any market's failure require some kind of compensatory State intervention. Quite the opposite, for them, market´s failures are less important than the reciprocal state's failures, being "the remedy worse than the disease". As a result of that way of seeing things, any State intervention would be negative. Given that, the presence of inappropriate markets regulations, excessive market concentration, regressive income distribution, or any similar problem, would not constitute is not a serious issue for neoliberals. Far worse would be any State´s intervention that attempts to correct that kind of malfunctioning.

The institutional blockades that have prevented progress in the deployment of a new development model, have given some weight to neoliberal criticism. The alleged "inefficiency of the State´s action" denounced by neoliberals, has been enhanced by the presence of institutional blockades to the non-neoliberal policies. To that fact, has been added an important lack of willingness to change on the part of the "progressive elite" and the capture from another part of it by the powerful neoliberal economic forces. Unfortunately, to date, the Chilean political system has been unable to deal adequately with these issues.

9.12. Neoliberalism as a Meta Institution

The neoliberal proposal that is in the roots of the Chilean model, has been acting as a meta-institution, i.e., an institution that structures the choices of institutions. Neoliberalism considers that human well-being can be better achieved by maximizing economic freedoms, within an institutional framework characterised by rights of private property, individual freedom, unfettered markets and free trade. Because of that, the neoliberal rules of the game act, in the Chilean context, as the central proposal securing that a certain coherence with the other (neoliberal) proposals is maintained. Playing a crucial role to safeguard functionality and coherence with neoliberal principles of the model of development implemented in Chile, and with the interests of larger business groups that control the economic life as a whole.

The Austrian school, which has inspirited original Chilean neoliberal proposals, already considered that some regularities, later interpreted as institutions, may emerge from

sequential interactions between agents, being advantageous to their interest and hence, preserved by them. Moreover, Hayek (1967) asserts that the market (or at least market rules) born from a cultural evolution process directed by a group selection mechanism in which relative prices play a core role. Within that point of view, in a manner very independent of the outcomes of economic model implantation, neoliberalism granted a conceptual order to building institutions. That order does not depend on operational success of established institutions, but on their consistency with the general institutional framework which neoliberal theory has defined as "the right one". Notwithstanding, the more radical neoliberal academic nucleus formed in Chicago supported that point of view, very soon the dominant stand point was influenced by a certain common sense permeated by politics. Given that, the central element that start to "sell" the Chilean neoliberal elite, was the success of its model in terms of its outcomes and not on the logical coherence of its proposals. On that basis, from the world of academia and multilateral organizations, "the success" of the Chilean model became exhibited as a reality beyond all discussion. Moreover, for many orthodox academics said "success" allowed them to assume that the neoliberal model, by not using "Austrian arguments" in its defence, could stop being defined as such, and begin to be denominated simply as a neutral economic model, structured on the basis of the "good economics" criteria.

Contrary to the vision of Hayek, the neoliberal order that emerged from the practical implementation of the Chilean model, clearly does not matched to some evolutionary course of action. On the contrary, it corresponds to an a priori design, which was imposed to the Chilean economy and society. This design has been embodied in a coherent group of neoliberal institutions and imposed from the political sphere. From that base, the neoliberal agenda has been consolidated in Chile, firstly using violence and then using the weakness of the new elite in power. All that was coupled with a constitutional iron-jacket that prevented any modification of the institutional structures constructed during the dictatorship period, at least without breaking the laws and the constitution inherited from the Pinochet´s period.

It currently allows (in the eyes of the people), that the quotidian economic order be understood as a structure independent of the violent origins of that order, weakening the citizen skill to perceive the actual relationship between causes and effects within the model of development in which they are immersed. This situation has made possible enlarge the political support of the neoliberal status quo in some sector of the population.

9.13. The Political Influence over Business Institutional Arrangements

At this point in time (2018), there is substantial evidence for the presence of a dense network of legislative compromises and financial support, established between large business groups, right wing political parties and also whit the leadership of progressive Chilean political forces who have come to power in 1990.

Those kinds of connections have obviously compromised the desire to change a model that provides substantial financial resources to both sides of the Chilean political class. However, that is only one side of the coin; the other is more ideological than pragmatic. In a significant part of the progressive political elite, a strong absorption of the neoliberal ideology has significantly diluted any reflection on the new role that the State should play in a market economy open to foreign trade and about the level of competition that should exist in the markets. This explains why, from the left wing, exist only a weak research or action agenda that exceeds the boundaries which has been imposed by the neoliberal thinking.

When this absorption of neoliberal thinking is combined with the presence of unequal levels of power in the process of political decision-making in Chile, both aspects exert a strong influence on the evolution of the economic development process.

The increasing dissemination of neoliberal ideas and abundant financial resources available to the economists, lawyers and politicians that define the rules of the economic game from that perspective, have produced a strong effect within the non-neoliberal political forces, limiting any intent to change income inequality or the extractive character of the economy through the political process.

That context is an expression of the low quality of a country's economic institutions, a situation that, in turn, adds force to the propensity of large business groups to be involved in rent seeking activities. This is the reason why the high predominance of the non-market activities of large business groups is a key variable that explains an important proportion of the slow Chilean evolution in productivity and its consequences on GDP growth and its distribution.

9.14. Creative Destruction or Creative Depredation?

The Chilean experience, reported in Chapter V, clearly shows that the prevailing Chilean institutions of economic governance, quite contrary to neoliberal promises, are not driving the Chilean economy towards a framework of market´s competition. In contrast, the real outcome of the Chilean model has been a massive concentration phenomenon, associated with a downgrade in the competition level existing in domestic markets.

The argument that concentration and market power would generate greater productive efficiency of the economy as a whole has become the basis of the development strategy promoted by Chilean Neoliberals. They have emphasised the need to allow the "modern" sector (large enterprises) to grow at the expense of the disappearance of the "traditional" sector (MSMEs). This strategic route has been "rationalized" under appeals to increase "creative destruction" in the Chilean economy.

This regressive process has been implemented from the high levels of the Chilean state, through the safeguarding of the institutional environment and through the application of spot macroeconomic measures that reinforce its effects. Additionally, to both mechanisms, the implementation of a predatory economic model that dominates the value chain has been cultivated as a desirable practice by large companies. It consolidates their market power and has, therefore, become a key part of the economic institutions of the Chilean economy as a whole.

This strategy has ended up generating an oligopolistic market structure that discourages technical progress, and absorption and diffusion of new technologies. In this context, corporations that are not operating in competitive markets, tend not to foster the use of innovation and productive improvement, which should be used as a mechanism to compete within each market. On the contrary, they promote the development of non-market activities. This is obviously a highly profitable strategy for these companies, but highly unproductive for the country.

All of this ends up discouraging the participation of large companies in external markets, especially when their participation requires productive efforts oriented towards the consumer.

Nevertheless, these companies, comfortably installed in quasi-captive internal markets, are moving in the opposite direction. Thus, as we have shown in this study, an outcome of mid-term is a drop-in productivity and a declining tendency in GDP growth rate.

Our findings show that trade liberalisation, market deregulation and the redefinition of the role of the State, combined with the adoption of an export-oriented development model based primarily on commodities, have not produced the expected results in terms of simultaneously boosting the economy and the living conditions of the Chilean population. In fact, practically all evidence reported in this dissertation, openly contradict the assessments and expectations of the neoliberal approach.

9.15. Why does the Neoliberal Model not work?

The three channels by means neoliberalism assumes which international trade affects productivity are:

1. Higher import intensity would expose domestic firms to competition, forcing them to raise their productivity and export intensity in order to survive in the market.
2. A higher level of imported inputs and capital goods would generate variations in the relative price of equipment. Allowing firms to optimise their productive processes and incorporate new technologies, in turn raising their productivity, especially if foreign technologies are more efficient than those available in the domestic market.
3. When trade openness is accompanied by FDI, the transfer of knowledge and learning by-exporting process, the economy would increase its productivity given the incorporation of new (foreign) firms using better practices in the technological area. However, the magnitude of this effect depends on the availability of skilled human capital, which really determines the capacity of domestic firms to adopt new technologies.

Our research has allowed us to conclude that none of these channels acts in the same manner that neoclassical economy predicts, and neoliberal promotes. The increased intensity of imports, the drop-in equipment prices and the large amounts of FDI that have been arriving to the country, have not translated into an increase of the number of exporting companies, nor into increase in economic productivity. Additionally, the country's TFP has fallen systematically to the extent that trade liberalisation has deepened.

The neoliberal forecast about their own outcomes fails, as its proposal does not incorporate the actual variables that condition the real mechanisms of the resource allocation and absorption of new technologies into the economy. Their belief that trade openness would be able to provide the autonomous adaptation of economic agents, accomplished through the markets in response to price signal following trade openness and market liberalisation, is a hypothesis, which has been clearly falsified during this research.

The conclusions that we have drawn from this research shows that the predominant mechanisms which determine relative prices in the Chilean economy are far from corresponding to those described in neoclassical theory. Prices defined by the real Chilean markets, are not functioning as a neutral and technical device. To the contrary, the performance of real markets that are consistent with neoliberal institutional arrangements, create domestic forms of resource allocation that are deeply unfair and inefficient.

The Chilean economy, frequently used as a model by the neoliberal and neoclassical economists, shows that the trade openness can result in stagnant or declining productivity, despite the fall in the prices of equipment. Even though it has sometimes resulted in technological improvements in the export industries of commodities intensive in natural resources, such improvements have not been achieved at the level of world-class production practices.

Thirty-seven years of opening has only slightly changed this situation, and the changes in relative prices induced by "openness" barely explains the evolution of technical progress. The large industries producing commodities that are intensive in natural resources (fish meal, pellets of iron, cellulose, nitrate etc.) show an evolution which seems to obey neither the prices system running on the markets in which they operate nor the market´s liberalisation process. The absorption and diffusion of technologies obeys determinants more complex than the single evolution of relative prices of such products and their inputs. Without real market competition and without the elimination of institutional barriers to progress for defiant economic actors, the economic efficiency of the Chilean economy will be very difficult target to achieve.

9.16. It is Bad Competition?

However, there are some Chilean industries operating in highly competitive environments, in first place, the MSME. If we disregard the presence of large firms, remembering that MSME comprise 98% of Chilean firms, almost 100% of firms would be operating in an extremely competitive context. Unfortunately, the very small size of these firms, combined with the activities used by large firms against them, does not produce a competitive framework that develops productivity and efficiency. In addition, there exists a small group of large and medium enterprises (wine, salmon, fresh fruit, services etc.) in which relative prices (external and internal) actually are playing a central role and in which, no doubt, trade openness has introduced and spread technical progress in a very powerful way.

In spite of this exceptional performance, non-traditional Chilean exports, mainly originated in those sectors, are little less than a third of total exports. Within this group, industrial exports (characterized by their low technological level and high intensity in natural resource (salmon, iron pellets, wines, fish meal, cellulose, processed wood, copper wires, etc.) are stabilised at around 33%. That situation is explained by the macroeconomic impact of mining exports, which generate a high influx of foreign currencies, appreciating exchange rate and generating a strong competitive handicap for enterprises operating in competitive markets, in which the prices, expressed in domestic currency are a key competitiveness factor.

The predominant domestic economic environment is one in which large companies obtain elevated profits without increasing competition, in which productivity is declining and insufficient innovation exists, and where the model is based on the exploitation of natural resources. In other words, evidence show that Chile has an institutional environment that generally is associated to a lack of long-term sustainability.

In conclusion, according to the results of our research, we can confirm the existence of sufficient evidence to state that beginning with trade openness in 1973, the national development of Chilean model began to undergo institutional transformations intended to consolidate the economic power of large business groups at the expense of the MSME and labour. Likewise, we contend that new post- dictatorship governments essentially maintain this neoliberal development strategy believing that in that way would be possible to sustain the impressive rates of growth that Chilean economy exhibit during the last decade of last century, an option that quickly proved not to be

true, but that defined the transitional nature of the Chilean political and economic life during the period 1990-2009.

9.17. The Quality of Institutions

Our findings show a stagnation of TFP, a growing gap between productivity and wages, a rise in the market power of large business groups, an ineffective allocation of prices and a serious lack in the capabilities of institutions to induce an inclusive and efficient operation of economic system. Given that, we may conclude that the general quality of the Chilean institutional framework is inadequate to produce a healthy openness-productivity-growth relationship.

It seemed important for us at this point to specify that institutional quality is crucial to foster the growth of the GDP, as well as the effectiveness of competition policy and the promotion of total factor productivity. Findings of worldwide research about that issue, allow us to conclude that competition policies are associated with better use of labour, and have synergies with innovation policies in countries that enjoy quality institutional environments, which is clearly not the Chilean case.

In the last decades, it has been gaining strength the point of view which sustain that institutional quality variations largely explain the differences in speed by which countries imitate and adopt technologies discovered at the frontier. Hence, the presence of differences in institutional quality between Chile and more developed countries becomes a variable of crucial importance in explaining the low presence of technology transfer from leading firms to eventual followers.

After having demonstrated in several areas the failure of the supposedly successful neo-liberal model implemented in Chile, we have shown how institutions are those who have played a central role in this failure. Institutional quality is of crucial importance in determining technology transfer from the leaders to the follower´s firms, however, frequently they act against productivity by producing very different outcomes than those promised in the neoliberal discourse.

The Chilean case shows how institutional quality, more than relatives prices, may act as an enhancing factor for technology transfers from the world frontier to those lagging behind, allowing the latter to theoretically catch-up with the leaders. Instead,

a country like Chile, which trails behind the technological level of more developed countries and, at the same time, in possession of poor institutions, has experienced, after a growth golden age, relatively lower GDP and productivity growth rates that act as a boundary to its convergence process.

Having an institutional framework of good quality acts as a factor that promotes growth, technological and social innovation in an economy, good institutions can induce good choices, info sharing and good distributional outcomes, while bad institutions can do the opposite. Our research results provide evidence for the hypothesis that at the actual development stage of the country, Chilean neoliberal institutions are inhibiting economic growth.

9.18. Concluding Remarks

This research has concluded that the outcomes of the Chilean neoliberal reforms have had little effect on the economic growth process. Our findings allow us to assume that in Chile- within a context of total openness, market liberalisation policies and a minimum role of the state- the resulting economic performance has been affected far more by the structure of political institutions and of economic governance than by the structure of relative prices.

The attempt to reallocate resources from the price system operates from the wrong side of the equation, since they are the institutions who play the essential role in this process. Despite this, it seems quite clear that the neoliberal emphasis on the pricing system, more than a policy proposal, has become a propaganda speech, which has allowed to large Chilean business groups to proceed to construct a scaffolding which, while defending the neutrality of a free price system, hides their domination over the institutional fabric. That kind of speech keep cover the LSE´s control over the process of allocation of resources and distribution of the profits of growth enabled by the extractive system. The possibility of positive outcomes being obtained in the future in that area, does not depend on the continuation of the Neoliberal model. On the contrary, launching a process of high GDP growth again will depend on the country's capacity to change the neoliberal model, simultaneously developing its capacity for consolidating a new institutional fabric.

In relation to the core question: Has the original neoliberal character of this model been preserved, after the end of dictatorship, without modifying its essential nature? in the course of our research, we have argued based on evidence that political institutions are crucial in determining existing boundaries to economic growth, especially when a country does not have a consolidated democracy.

The permanence of not fully democratic institutions generates a context in which these take the place of the process of democratic decisions making. This allows larger enterprises, economic business groups and politically right-wing lobbyists, to define, without major difficulties, the rules of the political and economic game.

Not addressing these crucial problems on the part of successive post-dictatorship governments, allows us to conclude that at the political level, the institutions inherited from the period 1973-1989, have maintained their essential traits and those that have been modified post 1990 are those that are not essential to preservation of neoliberal model. Given that is not possible demonstrate the presence of relevant changes to the core elements of the neoliberal model, it is sound assume that continuity widely predominates over discontinuity of it.

In economic terms, this conclusion is even more emphatic, because a new model of institutions of governance were neither built nor consolidated following the end of the dictatorship. Thus, whilst the neoliberal institutional environment has been inherited, institutional arrangements that have allowed this environment were based on post-dictatorship government decisions. The influence on the institutional environment and upon the governance institutions meant that there was little institutional difference, in the economic area, between the period when the country was under a dictatorial regime and when it was experiencing the fragile rebuilding of democratic mechanisms.

Our research showed that in Chile 1990-2009, powerful interest groups seized economic gains derived from democratisation; as long as the political institutions were not providing conditions that enlarged democratic mechanisms, they were able to reduce the power of dominant social groups, during the period under analysis and beyond.

The presence of solidly institutionalized non-democratic mechanisms generates high automation in the field of the linkages between companies of different sizes. Due to this situation, the concentration of demand and the segmentation of the supply of goods and services enables the generation of economic models, feeding highly regressive

wealth accumulation processes. In this context, the maintenance of undemocratic institutions in the post dictatorship context generates paradoxical political processes.

In order to avoid the radicalisation of social conflict, democratic political forces must first accept a non-democratic inherited institution, and secondly must accept that any change to the rules of the game might result in the deepening of political conflict with the far-right wing, engendering a new political and social conflict of abrupt and dangerous dimensions.

The answer to this institutional "Gordian knot" does not seem to simply be placed in the economic arena, but also the political. The re-activation of the social movements produced by student protests during 2006 and the breakdown of the progressive political coalition that took place in the 2009 presidential elections, dividing that coalition into two halves, has produced a movement that has begun to threaten the survival the neoliberal rules of the economic and political game. The combination of both processes has questioned, for the first time since 1990, the whole constitution of 1980 and the institutional environment built on it.

Without that kind of perspectives, that promote the need for institutional changes affecting the operation of the development model that Chile has been implementing, it appears difficult to untangle the aforementioned institutional knot. Whether Chile will be able to maintain its current path of economic progress, democratising its economic and social life, and maintaining at the same time a route of economic growth and social development, the neoliberal model may clearly be abandoned without any serious danger of authoritarian regression.

However, the institutional restructuring tasks, necessary to develop and consolidate a new development model, that allows overcoming the limitations of the neoliberal model.

Democratizing the Chilean economy and society, require that the Chilean political class build capacities far superior to those that they have exhibited during the period of transition from dictatorship to the actual semi-sovereign democracy, that characterizes Chile today. Unfortunately, these capabilities do not seem to have consolidated to the required levels. Without it, the most probable course of action is that the Chilean economy and society should continue making a harsh journey through the desert of the neoliberal institutional traps, which will not allow them to arrive easily to the promised land of development.

Samenvatting

Deze studie analyseert het economische beleid in Chili over de periode 1990-2009, waarbij is gekeken naar (a) effecten van de neoliberale handelspolitiek voor ontwikkeling van relatieve prijzen, productiviteit en concurrentiekracht, en (b) aanpassingen in instituties en van beleid die structurele economische veranderingen in gang zetten.

Voor de politiek-economische analyse van deze ontwikkelingen is een theoretisch kader uitgewerkt, dat op verschillende dimensies is getoetst met behulp van statische gegevens van de productiestructuur, huishoudbestedingen, bedrijfsinvesteringen, overheidsinkomsten en uitgaven, en handelsdata. Daarnaast is gebruik gemaakt van micro- economische modellen van factorproductiviteit en loonvorming, en macro-economische structuurmatrices en input-output analyses.

Op grond van een historische analyse van het Chileense neoliberale model (hoofdstuk 2) worden de aanpassingen in het sectorpatroon van de Chileense economie besproken (hoofdstuk 3), waarbij wordt geconcludeerd dat vrijhandel slechts bevorderlijk is voor een beperkt aantal bedrijven. Er is weliswaar sprake van economische groei, maar de beoogde convergentie van de Chileense economie komt nauwelijks van de grond (hoofdstuk 4).

Het liberale prijsbeleid en de sterke gerichtheid op internationale handel blijken ook maar beperkt bij te dragen aan de efficiënte allocatie van productiefactoren (hoofdstuk 5) en hebben daarnaast een averechts effect op de binnenlandse inkomensverdeling (hoofdstuk 6). Er is sprake van een economische ontwikkeling met structureel verschillende groei- en inkomenselasticiteiten.

De belangrijkste grondoorzaak van deze dichotomie is gelegen in de gesloten institutionele arrangementen binnen de Chileense bedrijvenstructuur (hoofdstuk 7), waardoor concurrentie beperkt blijft en er snel monopolies kunnen ontstaan. Bijgevolg loopt het neoliberale ontwikkelingsmodel vast in een netwerk van (politieke, economische, sociale, culturele en ecologische) 'institutionele valkuilen' (hoofdstuk 8).

Ter afsluiting wordt geconcludeerd dat in Chili gedurende de periode na de dictatuur niet is voldaan aan de centrale neoliberale hypothese dat vrije marktprijzen bijdragen aan grotere concurrentie en verbeterde efficiency. Belangrijkste oorzaak daarvan is dat de institutionele transitie geen gelijke tred heeft gehouden met de aanpassingen in het economische beleid. Daardoor is de bedrijvenstructuur sterk geconcentreerd en zijn technologische innovaties vertraagd (hoofdstuk 9).

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About The Author

Enrique Román is an economist, consultant and policy designer. He has had more than 30 years of professional experience designing and implementing programmes that increase competitiveness, including design and implementation of programs of business development services, financial services, matching grants programs, IT solutions, and public policies oriented to fostering of quality certification focused on MSME.

A common theme of his career has been helping governments and civil society organizations invest their resources more efficiently, especially those oriented towards the competitive development of MSMEs.

From 1990 to 1993 Enrique was advisor of the Chilean Minister of Economic Affairs and after that he held the position of head of investment promotion for CORFO, the Chilean Economic Development Agency, where he streamlined the allocation mechanisms of national government resources for productive development to the manufacturing and agro-industry sector. He also served as a member of the Board of Directors of the National Institute for Norms (the Chilean equivalent of the ISSO), the body responsible for setting and promoting the application in the Chilean enterprises of national standards of security, sanitation, consultant qualification, etc. During that period, he also was a member of the Board of Directors of several Chilean public enterprises. During the late nineties, he was advisor of Argentina´s Minister of Economic affairs, collaborating in creation of public programs of industrial reconversion and export promotion. Through the first decade of XXI century onwards, he served as a consultant to more than ten Latin American governments, several multilateral entities like the World Bank, the IADB, ILO, OEA, and to various international cooperation agencies and multiples NGOs involved in field work in sixteen countries in North, Central and South America.

In March of 2003 Her Majesty The Queen Beatrix of The Netherlands, appointed him as Officer of the Orange Nassau Order in recognition of his efforts in the economic development field and into the strengthening of relations between Chile and the Netherlands. From that year ahead, Mr. Román also participated in the design and creation of the Investment and Export Promotion Agency of Ecuador, and since 2007 to 2008 advise to Ecuadorian Ministry of Production and Competitiveness to provide a proposal of an industrial policy for the country. From 2010 to 2013 he was the CEO of "The Productive Network Project", located in Quito, Ecuador, oriented to increased

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